UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of	:	
	:	
JOHN THOMAS CAPITAL MANAGMENT GROUP LLC d/b/a PATRIOT28 LLC, GEORGE R. JARKESY, JR., JOHN THOMAS FINANCIAL, INC., and ANASTASIOS "TOMMY" BELESIS,	:	File No. 3-15255
	:	
Respondents.	:	

RESPONDENTS' OPENING BRIEF

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Dated: January 13, 2015

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STATEMENT OF THE ISSUES

1. The Administrative Proceeding is Void and the ALJ Erred in Concluding That the Commission had Not Invalidated the Proceedings in Violation of Respondents' Due Process Rights by Prejudging the Division's Allegations, Stripping from the Proceedings the Appearance of Fairness.

2. The Administrative Proceeding is Void Because the Commission's Exercise of Unguided Discretion in Selecting the Administrative Forum Was an Improper Use of Delegated Legislative Authority in Violation of the Separation of Powers Doctrine.

3. The ALJ Erred in Determining that Respondents' Rights to Equal Protection Under the Law Were Not Violated.

4. The Dodd-Frank Statutory Provisions Authorizing Imposition and Collection of Enhanced Penalties in Administrative Enforcement Proceedings Violate the Seventh Amendment.

5. The ALJ Erroneously Concluded that *Ex Parte* Communications Between the Division of Enforcement and the Commission Did Not Occur and Thus Did Not Violate Respondents' Due Process Rights.

6. The ALJ Erroneously Concluded that Respondents' Due Process Rights Were Not Violated Under the Doctrine of *Brady v. Maryland.*

7. Respondents' Rights to Due Process Were Violated Because of Respondents' Inability to Assert Counterclaims for Constitutional Violations and Respondents' Inability to Develop an Evidentiary Record of Such Violations in an Administrative Proceeding.

8. Respondents' Rights to Due Process Were Violated Because the Truncated Duration of an Administrative Proceeding Did Not Afford Respondents Sufficient Time to Prepare Their Defense.

9. The ALJ Erroneously Imposed Dodd-Frank Remedies Retroactively.

10. The ALJ Made Evidentiary Rulings, Findings of Fact and Conclusions of Law That are Clearly Erroneous and Constitute Prejudicial Error.

11. The ALJ Erred in Imposing Remedies Against Respondents that are Unsupported, Disproportionate, and Contrary to Public Policy.

STANDARD OF REVIEW

On the appeal of an Initial Decision, the Commission "performs a de novo review and can affirm, reverse, modify, set aside, or remand for further proceedings." *See* Office of Administrative Law Judges, About the Office, SEC, http://www.sec.gov/alj#.VFhqE_nF98E (last visited Nov. 3, 2014); *see also* 5 U.S.C. § 557(b).

INTRODUCTION

This administrative proceeding ("AP") against respondents George R. Jarkesy, Jr. ("Jarkesy") and JTCM (collectively, the "Respondents") is void due to prejudgment by the Commission. The pursuit of this AP has violated—and continues to violate—Respondents' constitutional rights to due process, equal protection and a trial by jury. Moreover, the decisional authority of the Commission and its staff, and the remedies sought in this proceeding, violate the constitutional separation of powers. The administrative law judge ("ALJ") has violated SEC procedures and the Administrative Procedure Act ("APA"), which invalidate the proceedings. The ALJ has also made numerous erroneous evidentiary rulings, findings of fact and conclusions of law, which fatally prejudiced Respondents. The sanctions recommended by the ALJ are contrary to law, unsupported by the evidence, out of proportion compared to the sanctions imposed on the settled co-respondents and in other similar cases, and are contrary to public policy. For these reasons, this AP should be dismissed with prejudice with no imposition of sanctions.

STATEMENT OF FACTS

JTCM and its manager, Jarkesy, formed two investment pools ("Funds") for wealthy, sophisticated persons to invest in highly-speculative investments, including equity investments and bridge loans to financially-troubled companies, and investments in insurance policies. Tr. 2380, 2385, 2391, 2394, 2399. The high and numerous risk factors were detailed at length in the offering memoranda ("PPMs"), including the risk of loss of the entire investment. Tr. 2386 – 88; Div. Ex. 206 at 2, 3, 20 – 32; Div. Ex. 210 at 7, 26 – 30. The PPMs were prepared by qualified counsel, and the investments were sold by a registered broker-dealer to its clients. Tr. 72 - 73, 2379 – 80, 2388, 2389, 2396 – 98. Some of the early Fund transactions were successful, and

JTCM made distributions of some of the Fund assets to investors. Tr. 2399, 2400. Much of the losses in the value of the Funds' assets occurred upon the failure of the portfolio companies, and the market crash in 2008 and 2009. Tr. 2407 – 2409, 2417, 2420 – 2421. The Division does not allege that Respondents misappropriated Fund assets—and they did not. *See generally* OIP (no claims of misappropriation). The losses in the Funds were caused by the market crash, not the alleged misrepresentations, such as the identity of the auditor or prime broker, the alleged mis-valuation of the assets or the alleged undisclosed relationship with the settled co-respondents. Tr. 2407 – 2409, 2417, 2420 – 2421.

Jarkesy invested $500,000 of his savings into the Funds. Tr. 31 – 32. He later withdrew $80,000, followed by loaning more than $100,000 back to the Funds. Tr. 2497 – 2498. Jarkesy lost money on the investment and did not receive any profit from the venture. JTCM received approximately $1.2 million in fees from the Funds, but had substantial expenses on behalf of the funds, such as transactional legal fees, accountant fees, auditor fees, staff and overhead, and travel expenses. Tr. 0064, Tr. 2405 – 2406.

ARGUMENT

I. The Proceeding is Void and the ALJ Erred in Concluding That the Commission had Not Invalidated the Proceedings in Violation of Respondents' Due Process Rights by Prejudging the Division's Allegations, Stripping from the Proceedings the Very Appearance of Fairness.

It is axiomatic that "[a] fair trial in a fair tribunal is a basic requirement of due process, *In re Murchison,* 349 U.S. 133, 136 (1955), and that principles of due process apply to administrative adjudications." S*ee Amos Treat & Co. v. SEC,* 306 F.2d 260, 264 (D.C. Cir. 1962). The Commission violated this basic requirement of due process by issuing an *ex parte*

order *finding* guilt months before *trying* the contested facts alleged against Jarkesy in the Order Instituting Proceedings ("OIP").

Before the Commission or ALJ considered any evidence, the Commission reached a settlement with co-respondents John Thomas Financial and Anastasios "Tommy" Belesis (together hereafter, "settled co-respondents") and issued an *ex parte* Order Approving Settlement that included 86 *findings of fact and conclusions of law against Jarkesy,* adjudicating the very allegations that due process demanded be given "a fair trial in a fair tribunal." This premature adjudication of Jarkesy's guilt, two months *before* the hearing on the merits, effectively resolved liability for all of the disgorgement and penalties sought by the Division in the OIP.

The Order Approving Settlement departed from the Commission's usual practice.[1] The SEC is empowered to settle pending enforcement actions by 5 U.S.C. § 554(e),[2] which simply requires entry of a "declaratory order" to memorialize the termination of the controversy. No authority permits inclusion of detailed *ex parte* findings of fact and conclusions of law against third parties.

It is well-established that the Commission should remain "neutral and detached adjudicator[s]." *Ass'n of Nat'l Advertisers, Inc. v. F.T.C.*, 627 F.2d 1151, 1168 (D.C. Cir. 1979). In *Antoniu v. S.E.C.*, 877 F.2d 721 (8th Cir. 1989), *cert. denied,* 494 U.S. 1004 (1990), a single SEC commissioner made published prehearing statements about Mr. Antoniu—who had recently been convicted of securities fraud—and commented favorably on the Commission's position in the AP against Antoniu *while* his statutory disqualification hearing before an ALJ was pending. *Id.* On the day the Commission issued its decision affirming the ALJ's initial decision granting a

[1] See http://www.sec.gov/litigation/admin/2013/34-70989.pdf

[2] 5 U.S.C. § 554(e), provides in its entirety that "[t]he agency, with like effect as in the case of other orders, and in its sound discretion, may issue a declaratory order to terminate a controversy or remove uncertainty."

lifetime ban, the commissioner recused himself, presumably from the final deliberation and Commission vote. *Id.*

The Eighth Circuit found the proceeding against Mr. Antoniu devoid of due process. *Id.* Noting first "the fundamental premise that principles of due process apply to administrative adjudications, [*s*]*ee Amos Treat & Co.,* 306 F.2d at 264," the court acknowledged that "[a] fair trial in a fair tribunal is a basic requirement of due process. Fairness of course requires an absence of actual bias in the trial of cases." *Antoniu*, 877 F.2d at 724.

The relevant inquiry was "whether [the] Commissioner[]'s post-speech participation in the ... proceedings comported with the appearance of justice." *Id.* The court concluded that the commissioner had "in some measure adjudged the facts as well as the law of a particular case in advance of hearing it;" it nullified all the Commission's proceedings, and it directed a new review of the evidence without any involvement by recused commissioner. *Id.* at 726.

Similarly, in *Texaco, Inc. v. Federal Trade Commission,* 336 F.2d 754 (D.C. Cir. 1964), *vacated on other grounds,* 381 U.S. 739 (1965), a commissioner gave a speech expressing the FTC's intent to crack down on anti-competitive practices. Stating a disinterested observer could conclude that the commissioner had "in some measure" prejudged the specific case before him, stripping from the proceedings the "very appearance of complete fairness," the court ruled that the commissioner's "participation in the hearing amounted in the circumstances to a denial of due process which invalidated the order under review." *Id.* at 760. In *Cinderella Career & Finishing Schools, Inc. v. Federal Trade Commission.*, 425 F.2d 583 (D.C. Cir. 1970), the court explained that,

> There is a marked difference between the issuance of a press release which states that the Commission has filed a complaint because it has 'reason to believe' that there have been violations, and statements by a Commissioner after an appeal has been filed which give the appearance that he has already prejudged the case and

> that the ultimate determination of the merits will move in predestined grooves. While these two situations—Commission press releases and a Commissioner's pre-decision public statements—are similar in appearance, they are obviously of a different order of merit.

Id. at 590.

Here, the *entire Commission* has issued a published Order that makes extensive *ex parte* findings that virtually all of the unproven allegations in the OIP *are true and correct,* and adjudges the Respondents to have violated the law as charged. The verdict was in before the trial began.

The Commission well understands the fatal effect of prejudgment bias in administrative adversarial proceedings. The Rules of Practice ("ROP") demand a "prejudgment waiver" *in advance of* every settlement of an AP, as well as in other circumstances that affect the settlement of an AP. 17 C.F.R. § 201.240. The validity of prejudgment claims is enshrined by this rule. In this case the Commission secured the required advance prejudgment waiver as to the settled co-respondents, but not as to the Respondents.

The Commission's prejudgment is not somehow avoided by the footnote in the Order Approving Settlement that the findings are 1) based upon Respondents' Offer of Settlement and 2) are not binding on any *other* person or entity in this or any other proceeding. It is clear that the Offer of Settlement is always drafted by the Commission (or its designees) and is fashioned in accordance with the established SEC format. To suggest that the Offer of Settlement is the work product of any respondent is ludicrous. Moreover—with only minor exceptions, none of which occurred here—respondents only consent to the SEC's jurisdiction over them and over the subject matter of the proceeding—not to the recitation of facts inserted in the offer or the order entered by the Commission. Regardless of how the terms of the settlement were reached and communicated, the Offer of Settlement is the product of the Commission. The footnote does not

disclaim prejudgment liability for the Commission; to the extent it has any legal effect, its reference to "other" persons or entities only underscores that the *Commission* is bound, and it is the Commission's prejudgment that has fatally tainted these proceedings.

. Jarkesy vigorously presented this grave error directly to the Commission, in one of several futile attempts to timely resolve the due process violations inside the administrative process, but the Commission, in its January 28, 2014, Order Denying Petition for Interlocutory Review, refused to even recognize the disqualification.

Under legal precedents, the ongoing administrative enforcement proceedings against Respondents are void—and have been since at least December 5, 2013. Because this AP lost it appearance of fairness and has been prejudged by the Commission, it is void and should be dismissed.

II. The Administrative Proceeding is Void Because the Commission's Exercise of Unguided Discretion in Selecting the Administrative Forum Was an Improper Use of Delegated Legislative Authority in Violation of the Separation of Powers Doctrine.

Respondents also challenge the Commission's decision to cast them into its internal courts as an exercise of legislative power that tramples the doctrine of separation of powers.

A. The Dodd-Frank Transfer of Coextensive Administrative Enforcement Authority to the Commission Constitutes a Delegation of Legislative Power.

Article I, § 1, of the Constitution vests "[a]ll legislative Powers herein granted ... in a Congress of the United States." *Whitman v. Am. Trucking Ass'ns,* 531 U.S. 457, 472 (2001) (quoting *Loving v. United States,* 517 U.S. 748, 771 (1996).) The courts have cautiously permitted delegations of legislative power to the executive branch only under limited circumstances. Government actions that "have 'the purpose and effect of altering the legal rights, duties, and relations of persons ... outside the Legislative Branch,'" constitute legislative

action. *Metro. Wash. Airports Auth. v. Citizens for Abatement of Aircraft Noise, Inc.*, 501 U.S. 252, 276 (1991). The decision-making surrounding agency adjudications "alter [ ] the legal rights, duties, and relations of persons ... outside the legislative branch," and involve "determinations of policy." *I.N.S. v. Chadha*, 462 U.S. 919, 952, 954 (1983) (discretion delegated statutorily to I.N.S. to decide whether to suspend individual immigrants' deportations by hearings before immigration judge, based on specified decisional criteria, was delegated legislative power). The delegated power of the Commission to institute administrative enforcement actions—instead of Article III actions—against targets clearly alters the legal rights, duties and relations of those targets. *See Thomas v. Union Carbide Agric. Prods. Co.*, 473 U.S. 568, 593 (1985) (agency administrative adjudications "surely determine liabilities of individuals").

Prior to Dodd-Frank, SEC enforcement actions against unregulated parties—ordinary citizens—seeking the imposition of harsh penalties were reserved to Article III courts, where targets received full constitutional protections, like the Seventh Amendment right to a jury trial and other vital procedural safeguards. Dodd-Frank's delegation to the Commission of administrative enforcement authority coextensive with judicial enforcement powers, coupled with undefined authority to choose an administrative forum to pursue the cases previously reserved to the judicial branch, vested the Commission with unprecedented power to determine the constitutional and procedural rights afforded to targets of enforcement action. Under Supreme Court separation-of-powers jurisprudence, the delegation to exercise this new administrative enforcement authority was legislative.

B. Congress May Transfer its Power to Assign Certain Statutory Enforcement Claims for Exclusive Adjudication in an Administrative Forum Only Where

it Imposes Specific Guidelines or an "Intelligible Principle" for Exercising that Delegated Authority.

To justify the power vested in Congress to designate certain categories of government claims for litigation exclusively in an administrative forum, the Supreme Court has deferred to the legislative branch and its judgment that the specialized expertise of regulatory agencies was necessary for the administration of the modern bureaucratic state. *See Granfinanciera, S.A., v. Nordberg*, 492 U.S. 33 (1989); *Atlas Roofing Co. v. OSHA*, 430 U.S. 442 (1977).

The Court has repeatedly stressed that "when Congress creates procedures 'designed to permit agency expertise to be brought to bear on particular problems,' those procedures 'are to be exclusive.'" *Free Ent. Fund v. Public Co. Accounting Oversight Bd.*, 561 U.S. 477, 489 (2010); *Whitney Nat'l Bank in Jefferson Parish v. Bank of New Orleans & Trust Co.,* 379 U.S. 411, 419-20 (1965). The boundaries required by the exclusivity of legislatively-created administrative procedures were uniquely lifted by Dodd-Frank, however, leaving it to the Commission to decide for itself which procedures are "to be brought to bear" in the enforcement of securities statutes.

Delegated agency decision-making must also be constrained by measurable standards, preventing agencies from usurping Congress' constitutional functions or misapplying the delegated power. The scope of the authority delegated defines the degree to which Congress must impose more or less detailed criteria to put an effective "leash" on the transferred power. *See Whitman,* 531 U.S. at 475 ("the degree of agency discretion that is acceptable varies according to the scope of the power congressionally conferred"); *Loving,* 517 U.S. at 772-773; *United States v. Mazurie,* 419 U.S. 544, 556-557 (1975). Congress must "clearly delineat[e] the general policy" an agency is to achieve and must specify the "boundaries of [the] delegated authority." *Mistretta v. United States,* 488 U.S. 361, 374 (1989). Congress must "'lay down by

legislative act an intelligible principle,'" and the agency must follow it. *Id.* at 372 (quoting *J.W. Hampton,* 276 U.S. at 406).

In Dodd-Frank, Congress has handed the Commissioners a blank check, providing no limits to confine or control the discharge of that authority. The transfer of that unconstrained and unreviewable legislative power violates the separation of powers, vitiating the underlying proceedings against Respondents.

C. In Delegating Authority to the Commission to Decide Which Categories of Enforcement Cases Will Be Adjudicated Administratively, Congress Failed to Provide an Exclusive Procedure or Any "Intelligible Principle" to Constrain the Commission's Decisions.

In SEC enforcement actions initiated post-Dodd-Frank, there is *no* statutory standard governing the exercise of executive decision-making in selection of a forum, nor is there any legislative history from which any "intelligible principle" can be divined by implication. The SEC admitted the lack of any statutory "intelligible principle" in the district court, stating:

> Congress . . . did not provide any criteria as when the Commission would or should do one versus the other [federal court action or administrative proceeding]. It's entirely left to the Commission's discretion. The Commission decides – does not have formal criteria. The Commission decides on a case-by-case basis, based on everything before it, which route it might want to follow.

Transcript of Hearing, January 31, 2014.

This does not comport with the rudiments of due process or the tenets of our constitutional structure. Where property and liberty interests are being adjudicated, due process requires a hearing on governmental action affecting those interests. *See Mathews v. Eldridge*, 424 U.S. 319, 334 (1976); *Armstrong v. Manzo*, 380 U.S. 545, 552 (1964). "The courts, when a case or controversy arises, can always 'ascertain whether the will of Congress has been obeyed,' *Yakus v. United States,* 321 U.S. 414, 425 (1944), and can enforce adherence to statutory

standards. *See Youngstown Sheet & Tube Co. v. Sawyer,* 343 U.S. 579, 584-87 (1952); *Ethyl Corp. v. EPA,* 541 F.2d 1, 68 (D.C. Cir.) (en banc) (separate statement of Leventhal, J.), *cert. denied,* 426 U.S. 941 (1976)." *Chadha*, 462 U.S. at 953-54. But in the case of the legislative power delegated to the SEC by Dodd-Frank, there is no way for an Article III court to "ascertain whether the will of Congress has been obeyed," because there are utterly no "statutory standards" to enforce.

The lack of any "intelligible principle" runs afoul of both the due process protections of the Fifth Amendment and the doctrine of separation of powers, invalidating the Commission's decision to prosecute its claims against Respondents in its own administrative tribunal. This Congressional grant of unconstrained power to the SEC is simply unconstitutional and cannot survive review.

III. The ALJ Erred in Determining that Respondents' Rights to Equal Protection Under the Law Were Not Violated.

The Staff arbitrarily chose to litigate the claims against Respondents in an AP rather than in federal court, which contravened Respondents' equal protection rights in two ways. First, the Division's decision violated Respondents' right to equal protection under the law by depriving them of their fundamental right to a jury trial guaranteed by the Seventh Amendment—subjecting the discrimination to strict scrutiny analysis. Second, the Division's decision has contravened Respondents' equal protection rights guaranteed by the Due Process Clause of the Fifth Amendment pursuant to the "class of one" doctrine. Thus, the Division's choice to place Respondents in the administrative forum, where *very* few respondents are successful, instead of

the courtroom, where the SEC enjoys a much more modest success rate,[3] has profoundly prejudiced Respondents.

The SEC has filed lawsuits in federal court against other unregistered individuals and entities for the same securities fraud violations under the *same sections* of the Securities Act of 1933, the Securities Exchange Act of 1934, and the Investment Advisers Act of 1940 that it is asserting against Respondents in this administrative process. These similarly-situated defendants—called "comparators" in equal protection parlance—are easily identified from public records, and nine such parties were specifically brought to the ALJ's attention.[4] These much more fortunate defendants are identical to Respondents in all *material* respects.

A. Denial of Respondents' Right to Trial By Jury Requires Strict Scrutiny Analysis.

The most obvious, and perhaps the gravest, consequence of the SEC's decision to prosecute Respondents in the AP setting rather than federal court is that it robbed Respondents' of their Seventh Amendment right to trial by jury,[5] which applies to securities fraud enforcement actions in Article III courts where the SEC seeks monetary penalties.[6]

"Strict scrutiny" analysis applies to discrimination in the exercise of a fundamental right. *See Skinner v. Oklahoma ex rel. Williamson,* 316 U.S. 535, 541 (1942) (Categorizing marriage

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[3] According to a recent study by *The New York Times*, in FY 2011 the SEC was successful in only 63% of its enforcement actions. *See* Gretchen Morgenson. *At the S.E.C., a Question of Home-Court Edge*, THE NEW YORK TIMES, Oct. 15, 2013, available at http://www.nytimes.com/2013/10/06/business/at-the-sec-a-question-of-home-court-edge.html.

[4] Attached hereto is Respondent's Exhibit A, a chart detailing the identities of the comparators, the dates of filing, the precise statutory violations alleged, and the federal district court in which each case was filed by the SEC.

[5] The Seventh Amendment provides that "In suits at Common Law, where the value in controversy shall exceed twenty dollars, the right of trial by jury shall be preserved, and no fact tried by a jury, shall be otherwise reexamined in any court of the United States, than according to the rules of the common law." U.S. CONST. amend. VII.

[6] In *Feltner v. Columbia Pictures Television, Inc.*, the Court expanded the Seventh Amendment jury trial right beyond determination of liability to the assessment of penalties as well: "[I]f a party so demands, a jury must determine the actual amount of statutory damages . . . in order 'to preserve "the substance of the common-law right of trial by jury."'" 523 U.S. 340, 355 (1998) (*quoting Tull v. U.S.*, 481 U.S. 412, 426 (1987).

and procreation as fundamental rights, and holding that "strict scrutiny of the classification which a State makes . . . is essential."); *see also Griffin v. Illinois,* 351 U.S. 12 (1956) (holding that a state law denying free transcripts to indigent convicted criminal defendants where the transcript was necessary to adequate and effective appellate review violated equal protection by discriminating against convicted defendants on account of their poverty, even though the Court has never treated poverty as a suspect classification); *Police Department of the City of Chicago v. Mosley,* 408 U.S. 92, 95-98 (1972) (using strict scrutiny analysis to strike down ordinance prohibiting all picketing near a school other than picketing involving a labor-management dispute under the Equal Protection Clause).

The Seventh Amendment should be recognized as a fundamental right, at least for purposes of equal protection analysis under the Fifth Amendment due process clause.[7] It is clear that "[t]he [Seventh Amendment] right to trial by jury 'is of such importance and occupies so firm a place in our history and jurisprudence that any seeming curtailment of the right to a jury should be scrutinized with the utmost care.'" *Chauffeurs, Teamsters & Helpers, Local No. 391 v. Terry,* 494 U.S. 558, 565 (1990) (quoting *Dimick v. Schiedt,* 293 U.S. 474, 486 (1935)). The Supreme Court has not considered the Seventh Amendment's status as a "fundamental" right since 1931,[8] long before the Court had even established the contemporary mode of analysis for

[7] While the Equal Protection Clause of the Fourteenth Amendment by its terms applies exclusively to the states, the Supreme Court has found a comparable equal protection component applying to the federal government in the Fifth Amendment's Due Process Clause. *See, e.g., Bolling v. Sharpe,* 347 U.S. 497 (1954).

[8] *See Hardware Dealers Mut. Fire Ins. Co. of Wisconsin v. Glidden Co.,* 284 U.S. 151, 158 (1931), where the Court declined, without discussion, to glean a jury trial right from the Fourteenth Amendment's *Due Process* Clause. The Court has recited the 1931 *Hardware Dealers* conclusion in more recent cases but without substantively revisiting the issue. *See Curtis v. Loethar*, 415 U.S. 189 (1974). In none has the Court addressed the Seventh Amendment's status as a fundamental right for Fifth Amendment equal protection purposes in the context of federal enforcement actions. *See also, In re Japanese Elec. Prods. Antitrust Lit.*, 631 F.2d 1069, 1085 (3rd Cir. 1980).

equal protection incorporation.[9] It is highly unlikely that the Supreme Court would ever be asked to face the issue of the Seventh Amendment's incorporation again, because forty-eight states have their own constitutional version of a right to jury trial in civil cases (the other two have statutory protections of the right), and the subtle differences among them have led the Supreme Court to avoid preempting the states' ability to implement those differences.[10] Thus, no negative inference, for purposes of equal protection analysis, should be drawn from the fact that the Seventh Amendment has never been incorporated through the Due Process Clause to apply to the states. Even a cursory examination of the history and purpose of the Seventh Amendment reveals that it is a fundamental right worthy of equal protection analysis.

The Declaration of Independence lists as one of the grievances against the English "depriving us in many cases, of the benefits of Trial by Jury." Thomas Jefferson wrote: "I consider [trial by jury] as the only anchor imagined by man, by which a government can be held to the principles of its constitution." 3 *The Writings of Thomas Jefferson* 71 (Washington ed. 1861). Justice Black once wrote that "[t]he founders of our government thought that trial of fact by juries rather than by judges was an essential bulwark of civil liberty." *Galloway v. United States,* 319 U.S. 372, 397 (1943) (Black, J., dissenting). Then-Justice Rehnquist reminded us that "[i]t is perhaps easy to forget, now more than 200 years removed from the events, that the right of trial by jury was held in such esteem by the colonists that its deprivation at the hands of the English was one of the important grievances leading to the break with England." *Parklane Hosiery Co., Inc. v. Shore,* 439 U.S. 322, 340 (1979) (Rehnquist, J., dissenting). Rehnquist admonished that "[t]he founders of our Nation considered the right of trial by jury in civil cases

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[9] The controlling standard for such incorporation is whether the right in question is "fundamental." *See, e.g., Duncan v. Louisiana,* 391 U.S. 145, 149 (1968).

[10] Uniform state protection of the right to jury trial strongly suggests that the right is fundamental.

an important bulwark against tyranny and corruption, a safeguard far too precious to be left to the whim of the sovereign...." *Id.* at 343 (footnote omitted). Historians have documented the centrality of the Seventh Amendment to the Bill of Rights. Indeed, the Framers saw the right to a jury in civil cases as so fundamental to ordered liberty that even before the delegates to the Constitutional Convention had left Philadelphia, plans were under way to attack the proposed Constitution on the ground that it failed to contain a guarantee of civil jury trial in the new federal courts. *Id.* at 341-42; *see also* Wolfram, *The Constitutional History of the Seventh Amendment,* 57 MINN. L. REV. 639, 662 (1973).

Of equal importance is the well-understood purpose of the right: "the civil jury is a cornerstone of democratic government, a protection against incompetent or oppressive judges, and a way for the people to have an active role in the process of justice." Moses, *What the Jury Must Hear: The Supreme Court's Evolving Seventh Amendment Jurisprudence,* 68 GEO. WASH. L. REV. 183, 183 (2000), citing Gunther, *The Jury in America,* xiii-xviii (1988); *see also* Klein, *The Myth of How to Interpret the Seventh Amendment Right to a Civil Jury Trial,* 53 OHIO ST. L.J. 1005, 1032 (1992) ("In 1789 there was a shared perception that guaranteeing the right to civil jury trials was important. Without an impartial jury, the individual citizen had no ability to check of the power of the sovereign in a civil courtroom."); *see also id.* at 1034 ("The principle captured in the amendment is that this specter of unchecked authority [in the courtroom] was unacceptable."). Noted English legal historian William Holdsworth explained the historical under-standing that the jury can bring "average common sense" to bear upon the facts in a way the judge could not. 1 William Holdsworth, *A History of English Law* 348 (6th ed. 1938). *See also* Note, *Developments in the law: The Civil Jury,* 110 HARV. L. REV. 1408, 1433 (1997), As on commentator argues, "the very fact that the civil jury is a democratic institution composed of

laypersons fosters a sense of inclusion and participation that reflects and generates popular endorsement of the judicial system. The citizen jury confers legitimacy on judicial actions by identifying the actions of government with those of the people, both actually and vicariously." Further, the Seventh Amendment right fosters "liberty, democracy, and political community." *Id.* at 1413.

In light of its history and purpose, the Seventh Amendment is no less "fundamental" for purposes of equal protection analysis than the rights to marriage and procreation, which are not even explicitly included in the Bill of Rights, but were still found "fundamental" in *Skinner,* such that— the state's denial of those rights to certain theft convicts but not similarly-situated others could not survive strict scrutiny. *Skinner*, 316 U.S. at 540-42. Additionally, the Seventh Amendment equally fundamental to the Second Amendment's right for an individual to bear arms, which was recently held to be fundamental and deemed incorporated. *McDonald v. City of Chicago,* 561 U.S. 742 (2010).

Because the discrimination against Respondents in the exercise of this fundamental right cannot survive strict scrutiny, the SEC's actions run afoul of Respondents' equal protection rights under the Due Process Clause of the Fifth Amendment.

B. Respondents are Entitled to Relief under the "Class of One" Equal Protection Doctrine.

There is no doubt that Respondents' Equal Protection rights have been trampled by the Staff's arbitrary decision to send them into the administrative process, where their ability to defend themselves has already been severely crippled. Within a few months of Respondents' case, the SEC has sued other identical targets in federal court, where all applicable Amendments and rules of procedure permit a defense on a level playing field. Under the so-called "class of

one" equal protection doctrine, Respondents are entitled to relief.

The "class of one" claim under the Fourteenth Amendment was first expressly recognized as such by the Supreme Court in *Village of Willowbrook v. Olech,* 528 U.S. 562, 564 (2000):

> Our cases have recognized successful equal protection claims brought by a "class of one," where the plaintiff alleges that she has been intentionally treated differently from others similarly situated and that there is no rational basis for the difference in treatment. . . . In so doing, we have explained that "'[t]he purpose of the equal protection clause of the Fourteenth Amendment is to secure every person within the State's jurisdiction against intentional and arbitrary discrimination, whether occasioned by express terms of a statute or by its improper execution through duly constituted agents.' "

(citations omitted). Earlier, in *Nordlinger v. Hahn,* the Court had explained that "[t]he Equal Protection Clause does not forbid classifications. It simply keeps governmental decision-makers from treating differently persons who are in *all relevant respects* alike." 505 U.S. 1, 8-9 (1992) (emphasis added).[11] Yet the Commission has treated Respondents "differently [from] persons who are in all relevant respects alike." The comparators are identical to Respondents in all material respects: all were charged with the same alleged violations and all could have been relegated to the administrative process, but were instead treated differently, for arbitrary, irrational and malevolent reasons.

The one published decision involving an equal protection claim in the context of the SEC's arbitrary choice of prosecutorial forums is *Gupta v. SEC.*, 796 F. Supp. 2d 503 (S.D.N.Y. 2011), in which Gupta complained of the Commission's decision to pursue its insider trading claims against him in an AP instead of federal court. Gupta identified a number of similarly-situated individuals whom the SEC also charged with insider trading but sued in federal court. *Id.* at 506. The court found that Gupta's "class of one" claim was sufficiently plead and that it satisfied the *Free Enterprise* test for federal intervention without requiring the exhaustion of

[11] The courts use "material" and "relevant" respects interchangeably.

administrative remedies. *Id.* at 513. The *Gupta* court pointed out that "even if the SEC were acting within its discretion when it imposed disparate treatment on Gupta, that would not necessarily exculpate it from a claim of unequal protection if the unequal treatment was still arbitrary and irrational." *Id.* Just as in *Gupta*, nothing here can exculpate the SEC from its unequal protection of Respondents, where the disparate treatment at the hands of the Commission was arbitrary, irrational and malevolent. The only remedy is dismissal of the AP proceeding.

IV. The Dodd-Frank Statutory Provisions Authorizing Imposition and Collection of Enhanced Penalties in Administrative Enforcement Proceedings Violate the Seventh Amendment.

All modern federal regulatory statutes include civil enforcement programs. In certain statutes, administrative agencies are given exclusive jurisdiction to adjudicate statutory violations and fashion remedies that may include fines or penalties. In other statutes, Congress has provided for both judicial and administrative enforcement. Where Congress has established separate judicial and administrative enforcement programs, penalty amounts have often been capped in APs, reflecting their remedial focus, but not in judicial programs in which punitive considerations affect penalty amount. If these administrative programs were to authorize an agency to adjudicate common law claims for which there would be a Seventh Amendment right to a jury trial, that statutory authorization would be unconstitutional on its face. *Cf. N. Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982).

Atlas Roofing Co. v. Occupational Safety & Health Review Commission, 430 U.S. 442, 453 (1977), held that Congress may constitutionally delegate to an executive agency authority to adjudicate compliance with regulatory requirements under a statutory provision that intertwines the grant of equitable relief with the assessment of remedial penalties. Adjudications of these

newly-created statutory "public rights" do not involve "'a suit at common law ... [nor are they] in the nature of such a suit. The proceeding is one unknown to the common law. It is a statutory proceeding.'" *Id.* at 453 (quoting *NLRB v. Jones & Laughlin Steel Corp.*, 301 U.S. 1, 48-49 (1937)). As a result, no jury is required to adjudicate such "public right" claims like the one in OSHA, where penalties are included in the remedial measures being adjudicated. *Id.* at 458-61.

In contrast, where Article III courts are authorized to assess civil penalties that may be punitive in nature under a provision that does not intertwine penalties with equitable remedies, adjudicating these penalties is grounded in common law and gives rise to Seventh Amendment rights. As the Supreme Court observed in *Tull v. United States*, "[a]ctions by the Government to recover civil penalties under statutory provisions ... historically have been viewed as one type of action in debt requiring trial by jury." 481 U.S. 412, 418-419 (1987). In holding that an action to impose civil penalties under the Clean Water Act involved resolution of a common law claim covered by the Seventh Amendment, the Court relied upon the "punitive nature of the relief sought" and the fact that the Clean Water Act enforcement section "does not intertwine equitable relief with the imposition of civil penalties. Instead, each kind of relief is separately authorized in a separate and distinct statutory provision." *Id.* at 425. The penalty provisions established by Dodd-Frank parallel the Clean Water Act penalties before the Court in *Tull.*

Dodd-Frank fundamentally changed SEC enforcement under the primary acts of the federal securities laws. Prior to Dodd-Frank, unregistered individuals in administrative enforcement proceedings only were subject to SEC non-punitive sanctions, like a cease-and-desist order. Dodd-Frank amended those statutes to authorize, in addition to equitable relief, separate and enormous civil penalties, and now allows the imposition of monetary "per violation" penalties that are identical to, *or greater than*, the statutory provision governing

judicially imposed civil penalties for identical securities law violations. Under the Securities Act, for example, maximum per-violation administrative penalties are 50 percent greater than what Article III courts may impose per violation.

In giving the SEC unprecedented power to assess the civil penalties that are punitive in nature and are imposed under a separate statutory provision focused exclusively on adjudicating liability for penalties (in contrast to a statutory provision, such as the one before the Supreme Court in *Atlas Roofing*, where penalties are intertwined with remedial measures), Dodd-Frank transformed the SEC administrative enforcement program for ordinary, unregistered persons like Respondents into a penalty-collection program that is indistinguishable from the Water Act penalty program before the Supreme Court in *Tull*. Because the Dodd-Frank administrative penalty provisions are functionally identical to the Clean Water Act provision in *Tull*, they violate the Seventh Amendment and render the pending administrative action against Respondents unlawful.

IV. The ALJ Erroneously Concluded that *Ex Parte* Communications Between the Division of Enforcement and the Commission Did Not Occur and Thus Did Not Violate Respondents' Due Process Rights.

A. The Commission and the Division Engaged in Impermissible *Ex Parte* Communication.

The ALJ erroneously concluded that the ex parte communications between members of the Division of Enforcement and the Commission in this proceeding were permissible and, thus, did not violate Respondents' due process rights. The authority relied upon for this conclusion is inapposite and inconsistent with the APA, the Commission's ROP, and the OIP in this case.

Persons involved in the investigation and prosecution of the AP also participated in the settlement discussions related to the co-respondents and recommended the settlement to the

Commission. This participation and recommendation constitutes improper ex parte communications. The OIP issued by the Commission in this case states:

> In the absence of an appropriate waiver, no officer or employee of the Commission engaged in the performance of investigative or prosecuting functions in this or any factually related proceeding will be permitted to participate or advise in the decision of this matter, except as witness or counsel in proceedings held pursuant to notice.

Respondents did not provide a waiver, did not receive notice, and were not permitted to participate or be heard in connection with the Commission's decision to settle with the settled co-respondents or its additional decision to enter findings and conclusions independently against Respondents. The communications between the Division staff and the Commission in resolving the claims as to the settled co-respondents without first procuring a waiver or giving notice and an opportunity to be heard by Respondents, violates the Commission's own admonition in the OIP, as well as the SEC's ROP and the APA.

The due process principles underpinning the proscriptions against *ex parte* input from Division staff have been applied to nullify proceedings even in exchange tribunals—to which the stricter standards of the APA do not apply. For example, in *Laken v. Chicago Mercantile Exchange*, CFTC No. 88-E-2, Comm. Fut. L. Rep. P 24,968 (Dec. 7, 1990), compliance staff representatives presented the case to the exchange adjudicators in a floor broker's disciplinary proceeding without the presence of the broker, and the Commodity Futures Trading Commission forcefully struck down the resulting sanctions. The CFTC acknowledged that

> [e]xchange proceedings are not subject to the strict separation of functions requirement applicable to Commission adjudications under the Administrative Procedure Act. *In re First Commodity Corporation of Boston*, [1986-1987 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 23,694 at 33,802 (CFTC May 29, 1987). Respondents in exchange disciplinary proceedings are, however, entitled to a fair trial in a fair tribunal. *Cf. In re Murchison*, 349 U.S. 133, 136 (1955). To be deemed fair, an exchange tribunal's actions must not only be free from actual bias, they must also be free from the appearance of bias. *Cf. Antoniu v. Securities and Exchange Commission*, 877 F.2d 721, 725–26 (8th Cir.1989) Generally, the

> test for an appearance of partiality is whether an objective, disinterested observer, fully informed of the facts, would entertain a significant doubt as to the fairness of the proceedings. *Id.*; *Pepsico, Inc. v. McMillen*, 764 F.2d 458, 460 (7th Cir.1985). When senior representatives of an exchange's Compliance Staff who played a substantive role in developing or presenting compliance's case are granted access to decision-making sessions of exchange adjudicators which are closed to respondent's representatives, an appearance of bias sufficient to offend fundamental fairness arises without regard to the precise role played by Compliance's representatives.

Id. at *8.

The Commission in *Laken* nullified the disciplinary decision, observing that the Exchange's claim that the involvement of the compliance staff in the adjudicatory recommendations was ministerial—not substantive—"would strain the credulity of the most trusting observer." *Id.*

In this case, the improper *ex parte* communications of the Division had exactly the impact that the language in the OIP was intended to prevent. Any claim that the Commission's extensive "findings" of fact against the Respondents were divined independently by the Commissioners without the benefit of input from the members of the Division working on the investigation and prosecution of the case, would "strain the credulity of the most trusting observer." The settling co-respondents neither admitted nor denied any of the factual conclusions in the Order Approving Settlement. It is clear that—however the terms of the settlement were reached and communicated—all Offers of Settlement are drafted by the Commission (or its designees) in the SEC's established format. Thus, the Commission either gleaned these facts from an illegal *ex parte* presentation by the Division, or the Commission simply conjured up the findings against Respondents out of thin air. Either prospect runs afoul of even the most rudimentary demands of due process and of the Commission's own rules.

The Division's participation in the Commission's findings against Respondents is a plain violation of the Commission's *very own Rules of Practice* and transgresses yet another

fundamental precept of due process. The Supreme Court has long held that rules promulgated by a federal agency that regulate the rights and interests of others are controlling upon the agency and must be followed by the agency. *Columbia Broad. Sys., Inc. v. United States,* 316 U.S. 407, 422 (1942); *see also, United States ex rel. Accardi v. Shaughnessy,* 347 U.S. 260 (1954). As the Second Circuit explained in *Montilla v. INS,* 926 F.2d 162, 169 (2d Cir.1991), "[t]he notion of fair play animating [the Fifth Amendment] precludes an agency from promulgating a regulation affecting individual liberty or interest, which the rule-maker may then with impunity ignore or disregard as it sees fit."

Section 554 of the APA states that, "This section applies, according to the provisions thereof, in every case of adjudication required by statute to be determined on the record after opportunity for an agency hearing...." 5 U.S.C. § 554(a). The agency's authority to enter into settlements provides, "The agency, with like effect as in the case of other orders, and in its sound discretion, may issue a declaratory order to terminate a controversy or remove uncertainty." 5 U.S.C. § 554(e).

Undoubtedly, the Division staff obtained a waiver from the settling co-respondents upon submission of the Division-drafted offer of settlement, as is required. Had Respondents made a written offer of settlement, they would have been required to give a prejudgment waiver before the Division of Enforcement staff engaged in communications with the Commission and its staff. Respondents gave no prejudgment waiver—nor was one requested—for the settlement communications regarding the co-respondents that resulted in entry of the December 5, 2013 order and press release in which the Commission made and published numerous adverse findings of fact and conclusions of law against Respondents.

B. *Stuart-James* and its progeny are not dispositive of the *ex parte* communication issue in this case.

In finding that improper *ex parte* communications did not occur between the Division and the Commission, the ALJ relied on *The Stuart-James Co.* and its progeny. *See* Initial Decision, p. 3. *Stuart-James*, however, is easily distinguishable from the matter at bar. *See* Exchange Act Release No. 28810, 1991 SEC LEXIS 168, at *2-18 (Jan. 23, 1991).

In *Stuart-James*, the Commission accepted a settlement that required a settling respondent to testify in accordance with the particular settlement entered. The non-settling respondents argued that by requiring the settling respondent to testify in accordance with the settlement papers, the Commission prejudged the matter because it intended to accept the testimony as true. *Id.* The Commission ruled that it had not prejudged the matter, because the non-settling respondents would be able to cross-examine the witness and impugn the witness's credibility and, should the matter pertaining to the non-settling respondents reach the Commission, it could decide the matter objectively by looking to the credibility of the testimony of the settling respondent. *Id.*

Respondents' situation is markedly different than that of the non-settling respondent in *Staurt-James*. First, the issue in this case does not pertain to a requirement that the settling respondents testify to establish some set facts to which they stipulated in exchange for a dismissal. In fact, *Stuart-James* did not pertain to any previous Commission findings, as the settling party received a dismissal in exchange for his testimony in accordance with his proffer of settlement—no findings of fact were issued by the Commission in *Stuart James*, and certainly no findings of fact pertaining to the non-settling respondents. In this light, the Commission did not pass judgment on any party, it merely agreed to the dismissal in exchange for future testimony. As the *Stuart-James* opinion notes, the Commission would evaluate the testimony and any impeachment evidence offered should the matter come back in front of the Commission. In this

matter, the Commission actually issued findings—based on impermissible *ex parte* contact—pertaining to the non-settling respondents.

Second, this case relates to conclusions of fact and law drawn by the Commission—influenced by the Division through improper *ex parte* discussions—that pertain to the non-settling Respondents, not the settling co-respondents.

Stuart-James establishes the following standard for determining prejudgment with relation to a non-settling respondent:

> [w]e agree with the respondents that they are entitled to an impartial and disinterested tribunal. However, there can be no prejudgment unless an agency has in some measure adjudged the facts in advance of hearing them.... The mere exposure to the "facts" of a case gained in the performance of an agency's statutory functions does not constitute prejudgment... We are mindful that permitting *ex parte* contacts concerning a pending settlement offer in a multi-party case poses a danger of abuse, *see Environmental Defense Fund v. EPA*, 548 F.2d 998, 1006 n.20. Discussions between us and the staff litigating a multi-party proceeding should be carefully circumscribed, so as to prohibit improper advice or influence with respect to a decision in the case against non-settling respondents.

Id., at *4-5. The Commission's findings in this matter go far beyond "mere exposure to the facts" and are a clear example of the Commission "in some measure adjudg[ing] the facts in advance of hearing them." In this matter, discussions between the staff and the Commission have not been "carefully circumscribed, so as to prohibit improper advice or influence with respect to a decision in this case against the non-settling respondents" as required by *Stuart-James*. Instead, the Commission, by virtue of its improper *ex parte* contact with the Division issued findings of fact pertaining to the non-settling Respondents; findings the Commission clearly gleaned from its *ex parte* contact with the Division as the stipulated agreement between the setting Respondents and the Commission contained no admission as to the facts or wrongdoing in the matter.

Further, the Commission has established an "act now and seek forgiveness later" standard with regard to determining whether impermissible *ex parte* contact with the Division occurred:

> The interests of non-settling parties in appearing at the presentation of a co-respondent's offer of settlement in an administrative proceeding must be balanced against the agency's own need to responsibly perform multiple functions as administrator, adjudicator and policymaker in assessing whether the settlement proposal is in the public interest. Whether or not *ex parte* contact between prosecuting staff and the agency heads is permissible depends, therefore, on what is discussed and for what purpose the discussion takes place.

Id., at *15. To determine whether the communications are in fact impermissible, the communications themselves must first occur. Put another way, for the Commission to glean whether the settlement is in the "public interest," the Commission must conduct what could later be determined to be *ex parte* communications with the Division, and subsequently the Commission must evaluate what was discussed and the purpose of the discussion to determine whether the *ex parte* contact should have occurred in the first place. Under this standard, there is no way for the non-settling respondents to challenge the *ex parte* contact before it occurs (as the Commission and Division do not even have to inform the non-settling respondents of the settlement discussions prior to their occurrence), and then, after the contact occurs, the Commission, in secret, determines whether it was in the wrong for communicating with the Division. All the while the non-settling respondents have no recourse against the Commission because its determination of whether it tainted the proceedings with impermissible *ex parte* contact is conducted in secret with no record to be reviewed by a disinterested and impartial court of appeals.

The non-settling respondents are left with only the hollow unsubstantiated representation by the Commission that the "[p]articipation of prosecuting staff in [the Commission's] consideration of [the settling Respondents'] settlement offer was carefully circumscribed" and that the "[p]rosecuting staff did not participate in, or advise in a decision with respect to the

disposition of the case with respect to [the non-settling Respondents]" though the only evidence available to the non-settling respondents—in this case, the findings of the Commission with regard to the settling party indicating that the Respondents violated the securities laws—screams otherwise.

V. The ALJ Erroneously Concluded that Respondents' Due Process Rights Were Not Violated Under the Doctrine of *Brady v. Maryland.*

The Division violated Respondents' constitutional right of due process by failing to comply with its obligations under *Brady v. Maryland* ("*Brady*"). The ALJ's conclusion otherwise is clearly erroneous and prejudicial error. See Initial Decision at 5-6.

A. The Division's Document Dump does not comport with *Brady* and its progeny.

The Division prevented Respondents from accessing the relevant evidence by effectively hiding it in a 700-gigabyte "document dump" without any effective means of identifying the contents. Producing millions of documents incapable of being searched reliably is no better than refusing to produce documents at all. Federal courts thus routinely hold that large, haphazard document productions violate the Federal Rules of Civil Procedure. S*ee, e.g., Residential Contractors, LLC v. Ace Prop. & Cas. Ins. Co.*, No. 2:05-cv-01318-BES-GWF, 2006 U.S. Dist. LEXIS 36943, at *7 (D. Nev. 2006) ("The Court does not endorse a method of document production that merely gives the requesting party access to a 'document dump,' with an instruction to 'go fish ....'"); *Mizner Grand Condo. Ass 'n v. Travelers Prop. Cas. Co. of Am.*, 270 F.R.D. 698, 700-01 (S.D. Fla. 2010) (granting defendants' motion to compel after plaintiff offered for inspection approximately 10,000 unsegregated and uncategorized documents that essentially required defendants to "examine and sort through each individual file folder").

The Division has been admonished in the past for using such tactics. In *SEC v. Collins & Aikman Corp.*, 256 F.R.D. 403, 413 (S.D.N.Y. 2009), the court required the SEC to produce 175 file folders created by its litigation attorneys. In reasoning applicable here, the court stated, "While the responsive documents exist somewhere in the ten million pages produced by the SEC, the production does not respond to the straightforward request to identify documents that support the allegations in the Complaint, documents [defendant] clearly must review to prepare his defense." *Id.* at 410. In *United States v. Skilling*, the court explained the proper procedure for making evidence accessible to parties faced with massive government data dumps:

> There is little case law on whether a voluminous open file can itself violate *Brady*, and the outcomes of these cases seem to turn on what the government does in addition to allowing access to a voluminous open file. *See, e.g., United States v. Ferguson*, 478 F. Supp. 2d 220, 241–42 (D. Conn. 2007); *United States v. Hsia*, 24 F. Supp. 2d 14, 29–30 (D.D.C. 1998); *Emmett v. Ricketts*, 397 F. Supp. 1025, 1043 (N.D. Ga. 1975). In the present case, the government did much more than drop several hundred million pages on Skilling's doorstep. The open file was electronic and searchable. The government produced a set of "hot documents" that it thought were important to its case or were potentially relevant to Skilling's defense. The government created indices to these and other documents. The government also provided Skilling with access to various databases concerning prior Enron litigation. . . . But considering the additional steps the government took beyond merely providing Skilling with the open file . . . we hold that the government's use of the open file did not violate *Brady*.

554 F.3d 529, 577 (5th Cir. 2009) *aff'd in part, vacated in part, and remanded on other grounds*, 130 S. Ct. 2896 (2010). Here, the SEC's Enforcement Division took none of the additional steps present in *Skilling*; the multiple databases and files produced are searchable, but only individually, meaning that several different databases and PDF files must be searched seriatim, adding to the monstrous chore of reviewing the data. No lists of "hot documents" were provided (or, if the lists exist, they were buried and not pointed out) nor were indices provided. If there was *Brady* material in the data the Division provided, it would take years for Respondents and

their counsel to adequately search through the data. Such a procedure does not comport with due process (or for that matter a meaningful disclosure of *Brady* material).

Subsequent to *Skilling*, a district court required the government to identify the *Brady* material in a multi-gigabyte, multi-million-page production. *United States v. Salyer*, Cr. No. S–10–0061 LKK (GGH), 2010 WL 3036444 at *4 (E.D. Ca. Aug. 2, 2010). In response to the government's argument that a *Brady* review would be an "impossible" burden, the court reasoned:

> During the course of the years long investigation in this case, the government personnel seemed to be able to segregate that evidence which would be useful in the prosecution in terms of guilt, but apparently made no efforts to segregate that evidence which runs counter to the charges. Assuming for the moment that some *Brady/Giglio* evidence, as the court has defined it below, exists, the reviewing personnel apparently made no note of the evidence, or merely having noted it, "stuck it back" in the ever-increasing pile to be an inevitably hidden part of the mass disclosure. The obligations imposed by Brady et al. have been well established for years, and should be anticipated in every case during the investigation phase. **If the government argues that it is now "impossible" to comply with the burden of reviewing evidence for identification purposes, the government more or less made its own bed in this matter by making it impossible.**

Salyer, 2010 WL 3036444 at *4 (emphasis added). Putting Respondents to trial with the opportunity to only review a miniscule percentage of the evidence that supported the issuance of the OIP—when the Division had *years* to comb through and evaluate the data before proceeding—is manifestly unfair and violates Respondents' rights to due process.

In dismissing the Respondents' *Brady* claims regarding the Division's document dump policies, the ALJ relied on two Commission opinions for the proposition that the Division's "open file" policy complies with *Brady*. *See* Initial Decision at 5-6. The only actual court authority mentioned is a footnote from the *Strickler v. Green*, 527 U.S. 263 (1999) case. However, the *Strickler* case did not determine that an "open file" policy comported with *Brady* obligations—only that in that particular case, the prosecution asserted that its *Brady* obligations

were met because it employed an open file policy. *See id.* The Court never passed judgment on whether the open file policy comported with *Brady*, and the Court certainly did not evaluate production with regard to a "data dump," as in *Residential Contractors, LLC*; *Mizner Grand Condominium Association*; *Collins & Aikman Corporation*; *Skilling*; and *Salyer*, discussed *supra*.

B. The Hearing Due Process Rights Were Violated When the ALJ Refused to Perform Required Duties Under *Brady* and its progeny.

In addition, the ALJ erroneously: a) concluded that Respondents' requests for interview notes were unfounded because she reviewed *some* of the interview notes and *the particular ones* that she reviewed contained no *Brady* material and b) failed to review, *in camera*, all documents that were claimed privileged, but may have contained *Brady* material. *See* Initial Decision at 5. The ALJ further refused Respondents' request to at least place copies of these documents under seal in the record as evidence and for an appeal. Because the SEC adopted *Brady*, it is obligated to follow that case and its progeny. As the SEC recognized in *In the Matter of optionsXpress, Inc.*, SEC Release No. 9466, AP File No. 3-14848 (October 16, 2013), a judicial officer's *Brady* obligation encompasses the *Pennsylvania v. Ritchie* duty to review, *in camera*, documents the government claims are privileged but may contain *Brady* material. The SEC's *Brady/Ritchie* obligations were specifically brought to the ALJ's attention, but she refused to review the notes in camera or make them part of the record for appeal.

Furthermore, the ALJ compounded the error by eliminating any possibility of Commission or appellate review of documentation in the custody of the Division that contained *Brady* material. Because the ALJ refused to follow *Brady* and *Ritchie*, Respondents not only were forced to the hearing without the *Brady* material that was almost certainly in the Division's possession, but Respondents also have no meaningful Commission or judicial review of the

erroneous decision because the *Brady* notes are not in the record, and Respondents will therefore be unable to demonstrate the materiality of the denied evidence.[12]

VI. Respondents' Rights to Due Process Were Violated Because of Respondents' Inability to Assert Counterclaims for Constitutional Violations and Respondents' Inability to Develop an Evidentiary Record of Such Violations in an Administrative Proceeding.

Respondents have alleged sufficient facts—uncontroverted by the SEC—to establish that the Commission's December 5, 2013, order containing some 86 findings of fact against them and one incriminating conclusion of law against them, just as alleged in the OIP, constituted prejudgment and rendered the AP void. Discovery is necessary in support of evidence-based constitutional claims, such as an equal protection claim, where the gathering of the facts is necessary "to further elucidate the essential issues of th[e] case... ." *Miller v. Caldera*, 138 F. Supp. 2d 10, 12 n.1 (D.C. Cir. 2001). *See also, Greater Baltimore Ctr. for Pregnancy Concerns, Inc., v. Mayor & City Council of Baltimore*, 721 F.3d 264, 282 (4th Cir. 2013) (to properly adjudicate constitutional challenge in an as-applied analysis, the district court was obliged to first afford discovery). However, there can be no adequate evidentiary record on which Respondents can present their equal protection, prejudgment and *ex parte* communications claims to the Commission or later to a circuit court under the statutory review process dictated by the APA and the Commission's Rules of Procedure (the "ROP").

There is no procedural mechanism for the necessary development of evidence in support of the claims under the SEC's ROP or the APA. Just as in *Gupta,* for these evidence-based

[12] Further evidence of the ALJ's and Commission's inability to adjudicate constitutional claims is supplied by their conclusions to Respondents' motions regarding *Brady* material. In an incredible misapplication of *Brady* and its progeny, the Commission's December 6, 2013, order [Securities Act Release No. 9492] concluded that evidence in the Division staff's notes was not *Brady* material because it did not *impeach Respondents.*

claims, judicial review (in the circuit court alone) is therefore impossible. There is no way to create the necessary record to establish the claim for appellate review. The *Arjent* and *Gupta* courts pointed out the obvious—that the SEC's administrative process provides no mechanism for developing the evidence necessary to sustain such a claim. *Arjent LLC v. Sec. & Exch. Comm'n*, 7 F. Supp. 3d 378, 384 (S.D.N.Y. 2014); *Gupta,* 796 F. Supp. 2d at 513. This point was underscored as Respondents nevertheless engaged in a quixotic attempt to litigate their equal protection claim in the AP, petitioning the ALJ for subpoenas for the production of records in support of the claim. The ALJ summarily denied the subpoenas after the Enforcement Division objected that the equal protection issues—along with the other constitutional claims—were of "absolutely no relevance" to the administrative process.

To the extent that the prejudgment claim is not already clearly established by the Commission's December 5, 2013, order, discovery, denied by the ALJ, is necessary to establish the circumstances of the Commission's premature decision against Respondents and the unlawful, *ex parte* participation of the Enforcement Division.

Unfortunately, neither the architecture of the APA's administrative adjudicatory process nor the ROPs provide any means for pursuing these evidence-based "as applied" claims in an AP, thus providing no avenue of appellate review—much less "meaningful" review—through the statutory review process, in violation of Respondents' constitutional rights. The Commission's previous assertion that "the Commission's *de novo* review following the issuance of an initial decision will offer an adequate forum for JTCM and Jarkesy to present their constitutional claims" is simply untrue. With no evidentiary support for the claims, no such "meaningful" review can occur.

VII. Respondents' Rights to Due Process Were Violated Because the Truncated Duration of an Administrative Proceeding Did Not Afford Respondents Sufficient Time to Prepare Their Defense.

The APA, 5 U.S.C. § 551 *et seq.*, under which the SEC Rules of Practice are promulgated, requires, as a matter of fundamental fairness and just adjudication, that parties must be "timely" informed of "the matters of fact and law asserted." 5 U.S.C. § 554(b). "Just determinates" are prescribed by the SEC in APs. 17 C.F.R. § 201.103(a). An inadequate opportunity to discover the relevant facts upon which the proceeding will be decided, given insufficient time to diligently pore through millions of pages of unorganized documents, deprives Respondents of rudimentary due process and their right to meaningful and effective confrontation of witnesses. *See Davis v. Alaska*, 415 U.S. 308 (1974). These principles are relevant to the fundamental fairness of APs where a respondent may be fined or otherwise sanctioned. *See Locurto v. Giuliani*, 447 F. 3d 159 (2d Cir. 2006) (party in hearing before administrative law judge does not receive "a full and fair opportunity to litigate" where he was "denied adequate discovery" on the relevant issues); *see also Veleron Holding, B.V. v. Morgan Stanley*, No. 12 Civ. 5966, 2014 WL 1569610, at *13 (S.D.N.Y. Apr. 2, 2014) (finding the opportunity to litigate "is neither full nor fair" where discovery more limited than that of a court).

Respondents were materially harmed by this inability to prepare in preparation for the evidentiary hearing, and informed the ALJ that they were not adequately prepared to cross examine the Division's witnesses and to present their defensive evidence. Forcing Respondents to an adversarial evidentiary hearing with the opportunity to only review a miniscule percentage of the evidence that supported the issuance of the OIP is manifestly unfair and violates Respondents' rights to due process. This is especially true where, as here, the Division has had

years to review the same documents in determining whether to bring claims against Respondents.

VIII. The ALJ Erroneously Imposed Dodd-Frank Remedies Retroactively.

The effective date of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank") was July 21, 2010. *See Weller v. HSBC Mort. Servs., Inc.*, 971 F. Supp. 2d 1072, 1077 (D. Colo. 2013). The Initial Decision erroneously imposed a monetary penalty on Respondents for conduct that predates Dodd-Frank in violation of the well-established rule that a statute will be presumed not to impose penalties retroactively unless it expressly so states. *See Landgraf v. USI Film Prods.*, 511 U.S. 244 (1994). Many of Respondents' actions at issue, [including,] happened prior to the effective date of Dodd-Frank, which may not be applied retroactively. *See Henning v. Wachovia Mortg.*, 969 F. Supp. 2d 135, 146 (D. Mass. 2013) (providing a list of cases ruling that the provisions of Dodd-Frank do not provide for retroactive application).

The ALJ's reliance on the theory of a "continuing course of conduct" is unsupported and inconsistent with applicable law. *See Landgraf*, 511 U.S. at ___ (refusing to apply remedies under the Civil Rights Act to allegedly violative conduct occurring prior to the law's effective date); *Miller v. Cbc Cos.*, 908 F. Supp. 1054 (D.N.H. 1995) (refusing to apply remedies under the Americans with Disabilities Act to allegedly violative conduct occurring prior to the law's effective date. The ALJ's cursory dismissal of Respondents' argument against the retroactive application of the law based on a continuing course of conduct is *exactly* what the *Landgraf* opinion sought to foreclose.

IX. The ALJ Made Evidentiary Rulings, Findings of Fact and Conclusions of Law That are Clearly Erroneous and Constitute Prejudicial Error.

The ALJ made numerous and repeated erroneous evidentiary rulings throughout the hearing that constitute prejudicial error. The ALJ's reliance on a record resulting from the inconsistent and capricious admission of Division evidence and exclusion of Respondent evidence underlies the erroneous findings of facts and conclusions of law.

(a) Erroneous Evidentiary Rulings

The ALJ's numerous erroneous rulings include admitting business-records affidavits offered by the Division that are facially defective, compounded by admitting the hundreds of unauthenticated documents which the defective affidavits purported to sponsor, and further compounded by relying on the interpretation of the contents of the documents attributed by the Division with no qualified sponsoring witness. Respondents objected to the admission of all of the business-records affidavits due to their defects, and objected to the admission of the associated documents for a lack of foundation. Moreover, there was no evidence that document custodians were unavailable to testify. Virtually all of the unauthenticated, unsponsored documents were admitted and now contribute to the erroneous findings of fact and conclusions of law in the Initial Decision.

Despite the lenience shown by the ALJ in accepting the facially-defective affidavits offered by the Division, the ALJ excluded the affidavit of settled co-respondent Anastasios "Tommy" Belesis offered by Respondents. The Division objected, arguing that Respondents had not demonstrated that Belesis was unavailable to testify, even though the Division conceded that Mr. Belesis would invoke his Fifth Amendment privilege if subjected to cross-examination by the Division, thereby making him unavailable.

The ALJ issued a subpoena at the request of the Division several days after the start of the hearing and allowed the Division to call a witness—Arthur Coffey—who had never before appeared on any witness list. Respondents objected to the testimony of the witness as unfair due to lack of adequate notice and opportunity to prepare. The ALJ allowed the testimony. Respondents were not given adequate time to prepare for cross examination—such as by conducting a search through the 700 gigabytes of data produced by the Division—but were required to cross-examine the witness immediately due to the witness' unavailability because of a personal matter.

The ALJ refused to issue the subpoenas prepared by Respondents to the investors on the Division's witness list, and instead edited *sua sponte* all of those subpoenas. Despite no filing of a motion to quash or modify the subpoenas, the ALJ determined on her own motion that the subpoenas were "unreasonable and oppressive" in their request for the investors' tax returns and statements for investment accounts for the prior five years. The ALJ stated in an order, "[t]he excluded items contain confidential information that is *completely irrelevant to the investors' expected testimony or any issue in this proceeding*." (emphasis added) AP Ruling Release No. 1035, November 12, 2013. It is impossible to conclude that the testifying investors' investment experience and personal financial condition during the relevant period is viewed as "completely irrelevant" in a case where offering fraud is charged. These witness' status as "accredited" and "sophisticated" and risk-tolerant investors were an issue in the case.[13] In addition, in a case

[13] It should be noted that in FINRA arbitration disputes, the following documents are listed in the Discovery Guide as relevant *per se* in disputes between a firm and a customer: 1) customer tax returns for the period starting three years *prior* to the first transaction at issue, and 2) customer financial statements including statements reflecting assets, liabilities and net worth for the period starting three years *prior* to the first transaction at issue. See FINRA Discovery Guide available at http://www.finra.org/web/groups/arbitrationmediation/@arbmed/@arbtors/documents/arbmed/p394527.pdf

where penalties are sought, the level of the investor's vulnerability versus sophistication is relevant to any analysis of the degree of egregiousness of conduct. Here, Respondents were forced to conduct the hearing without the ability to demonstrate the level of wealth, investment sophistication and risk tolerance possessed by the investor witnesses.

The ALJ also edited *sua sponte* the subpoena issued by Respondents to settled co-respondent Mr. Belesis, who was included on the Division's witness list. The ALJ eliminated the same financial records as for the testifying investors. Numerous financial transactions involving all respondents were at issue, and Respondents were left to try to defend the case without access to the records for those transactions. Moreover, in a case where aiding and abetting is charged and penalties are sought, the relative culpability of the settled respondents versus the Respondents is at issue.

The ALJ refused to authorize issuance of a subpoena by Respondents for SEC records needed related to Respondents' constitutional claims, thereby preventing Respondents from obtaining the evidence needed to support their evidence-based, as-applied constitutional claims. This prevented Respondents from creating the necessary record for these claims to be reviewed upon appeal of the Final Decision to U.S. Court of Appeals.

The ALJ made numerous other inconsistent evidentiary rulings, liberally allowing evidence offered by the Division and excluding evidence offered by Respondents. She admitted documentary and witness testimony over hearsay objections by Respondents, stating that hearsay is no barrier to admission in APs, and then excluded Respondents' evidence sustaining the Division's hearsay objections.

Each of these erroneous evidentiary rulings was prejudicial to Respondents and, separately and cumulatively, fatally undermined the integrity and outcome of the AP.

(b) Erroneous Factual Findings

Numerous of the allegations in the OIP were either proven false or not supported by credible evidence during the hearing. For example, the private placement memoranda themselves proved that Fund II was always open to domestic investors, that Fund II was not scheduled to expire or terminate in September 2012—and therefore Respondents were not late in distributing the assets, and that the durations of both funds could be extended at the election of the Manager. Other documents demonstrated that the values attributed to both funds at the end of 2011 were wrong—by a wide margin. However, instead of recommending dismissal of the proceeding for failure to substantiate the allegations in the OIP, the ALJ made many factual findings in the Initial Decision that were not alleged in the OIP, thereby giving Respondents no fair notice of these accusations.

For example, the ALJ based the conclusions of law and sanctions on target ownership percentages in the private placement memoranda ("PPMs") related to insurance policies, when there is no mention of this in the OIP. The ALJ then ignored the terms of the PPM that permit adjustment to the asset mix and strategy—like upon the occurrence of a market crash such as the one that occurred in 2008 and 2009. Further, the ALJ relied upon the PPMs for the terms that supported the Division's theory, improperly ignoring the rest of the terms, calling the discussion of risk factors "boiler plate." This selective reliance upon the PPMs is wholly improper and a misapplication of the law.

The ALJ made numerous erroneous and unsupported findings of fact, especially based upon the unreliable and unauthenticated documents admitted into evidence, including the following:

The ALJ erroneously concluded that an undisclosed relationship exists between Respondents and the settled respondents, John Thomas Financial ("JTF") and Anastasios

Belesis ("Belesis"). Initial Decision 16. This finding is not supported by credible evidence and ignores contradictory evidence that they acted independently.

The ALJ erroneously concluded that the selection of the name for John Thomas Financial was serendipitous. Initial Decision 9. This finding mischaracterizes the evidence and ignores contradictory evidence.

The ALJ erroneously concluded that Belesis and Jarkesy became acquainted in 2003. ALJ further erroneously concluded in a footnote that Jarkesy denied that date but did not provide an alternate date. Initial Decision 8. This finding mischaracterizes the evidence and ignores and excluded contradictory evidence of the correct date offered by Respondents.

The ALJ erroneously concluded that Belesis reinforced his position in the relationship through threats to stop selling interests in Jarkesy's Funds. Initial Decision 10. This finding mischaracterizes the evidence and ignores contradictory evidence.

The ALJ erroneously concluded that Jarkesy testified in an evasive manner that did not provide any assurances of the reliability of his testimony. Initial Decision 10. These findings mischaracterize Jarkesy's testimony.

The ALJ erroneously concluded that while Jarkesy evaded a large portion of the Division's questions, his recollection markedly improved when questioned by his own counsel. Initial Decision 11. This finding mischaracterizes Jarkesy's testimony.

The ALJ erroneously concluded that some of the representations in the marketing materials may have been accurate when the documents were first used became inaccurate and were not corrected. The ALJ further erroneously states that Respondents argue that the Division did not prove that the private placement memoranda were used without alteration throughout the time at issue. However, Respondents, who are in the best position to know of any successor PPM amendments, did not offer evidence of any changes. The ALJ further erroneously found that the private placement memoranda were used without further amendments in selling interests in the Funds during the time in issue. Initial Decision 11. These erroneous findings mischaracterize the evidence—including express authority to change professionals, business plan and asset mix—and Respondents' legal obligations and the applicable burden and standard of proof.

The ALJ erroneously concluded that investors might be able to redeem their investments, but upon potential payment of a penalty. Initial Decision. Initial Decision 12. This

conclusion mischaracterizes the evidence, the written terms of the investment, relies on unreliable evidence and ignores contradictory evidence.

The ALJ erroneously concluded that investor Robert Fulhardt believed that the Fund has a September 2012 maturity date, and investor Steve Benkovsky also believed that the fund had a five-year duration that would end in 2012. Initial Decision 12. These findings mischaracterize the evidence—including the written terms of the investment—rely on unreliable evidence and ignore contradictory evidence.

The ALJ erroneously concluded that in a podcast sent to investors on May 21, 2009, Jarkesy explained that uses of investment capital by percentages. Initial Decision 13. This conclusion mischaracterizes the evidence, relies on unreliable evidence, ignores contradictory evidence and misapplies the law.

The ALJ erroneously concluded that remaining portion of funds after life insurance policies were bought was to go to medium term debt and equity in business enterprises. Initial Decision 13. These findings mischaracterize the evidence—including express authority to change business plan and asset mix—relies on unreliable evidence and ignore material other evidence.

The ALJ erroneously concluded that the PPM for Fund II did not provide such numerical details. However, marketing materials for Fund II represented that about half of Fund II's investment would be in insurance policies amounting to at least 117% of capital commitments with additional funds to secure payment of premiums with the other half in corporate investments. Initial Decision 14. These findings mischaracterize the evidence, the written terms of the investment, rely on unreliable evidence and ignore contradictory evidence.

The ALJ erroneously concluded that contrary to the representations in the Funds' PPMs and financial statements that JTCM set the valuations for the Funds' positions, Jarkesy disclaimed responsibility tor this, indicating that AlphaMetrix valued the Funds' positions. The ALJ made additional erroneous conclusions regarding who participated in valuing assets and how assets were valued. Initial Decision 15. These findings mischaracterize the evidence, rely on unreliable evidence and ignore material other evidence.

The ALJ made erroneous conclusions regarding the role of KPMG and Deutsche Bank and the representations about them to investors. Initial Decision 15. These findings mischaracterize the evidence—including express authority to change professionals and the business plan—rely on unreliable evidence and ignore material other evidence.

The ALJ erroneously concluded that some statements in the PPM may have been accurate when made, became inaccurate and remained uncorrected. Initial Decision 11. These findings mischaracterize the evidence—including express authority to change professionals and the business plan—and mischaracterize the law and duties applicable to Respondents.

The ALJ erroneously concluded that Financial Statements represented valued according to FAS 157. Initial Decision 14. This finding mischaracterizes the evidence, relies on unreliable evidence and ignores material other evidence.

The ALJ erroneously concluded that valuation of each asset in the Funds' holdings was listed on each Funds' holdings pages, and that each investor's share was calculated from those holding pages. Initial Decision 14-15. These findings mischaracterize the evidence, rely on unreliable evidence and ignore material other evidence.

The ALJ erroneously concluded that Alphametrix did not participate in valuing the funds. Initial Decision 14. This finding mischaracterizes the evidence, relies on unreliable evidence and ignores material other evidence.

The ALJ erroneously concluded that any question concerning valuation would go to Jarkesy (through subordinates at times) and Jarkesy had the final word setting valuations, even if unreasonable. Initial Decision 15. These findings mischaracterize the evidence, rely on unreliable evidence and ignore material other evidence.

The ALJ erroneously concluded that JTCM approved all statements – holdings, profit and loss, financial statements, and investor statements. Initial Decision 15. These findings mischaracterize the evidence, rely on unreliable evidence and ignore material other evidence.

The ALJ erroneously concluded that on December 12, 2009 Belesis ordered Jarkesy to deliver funds and on December 18 Fund I bought $30,000 in Galaxy stock and Fund II bought $10,000 in Galaxy stock. Initial Decision 17. These findings mischaracterize the evidence, rely on unreliable evidence and ignore material other evidence.

The ALJ erroneously concluded that inconsistent with the PPM, Fund II bought no life insurance policies. Initial Decision 22. These findings mischaracterize the evidence, rely on unreliable evidence and ignore material other evidence.

The ALJ erroneously concluded that Fund I did not meet 117% obligation in 2008. Initial Decision 22. This finding mischaracterizes the evidence—including express authority to change business plan and asset mix—relies on unreliable evidence and ignore material other evidence.

The ALJ erroneously concluded that Fund I did not meet 117% obligation in 2010. Initial Decision 23. This finding mischaracterizes the evidence—including express authority to change business plan and asset mix—relies on unreliable evidence and ignores material other evidence.

The ALJ erroneously concluded that Respondents did not spend the amount pledged on insurance policies/premiums; nor put the policies in the master trust in a timely fashion as promised in the PPM and marketing materials. Initial Decision 23. These findings mischaracterize the evidence—including express authority to change business plan and asset mix—rely on unreliable evidence and ignore material other evidence.

The ALJ erroneously concluded that Respondent purchased policies at 15% rate, but valued at 12% rate. Initial Decision 24. These findings mischaracterize the evidence, rely on unreliable evidence and ignore material other evidence.

The ALJ erroneously concluded that Respondent immediately wrote up the value of policies in contravention of FASB Staff Position 85-4-1. Initial Decision 24. These findings mischaracterize the evidence, rely on unreliable evidence and ignore material other evidence.

The ALJ erroneously concluded that Jarkesy represented to investors that Fund I continued to purchase insurance policies in an August 2010 letter to investors which was a misrepresentation because Fund 1 never acquired a policy after 2009 year end. Initial Decision 24. These findings mischaracterize the evidence, rely on unreliable evidence and ignore material other evidence.

The ALJ erroneously concluded that Respondents represented the insurance policies as a conservative hedge but took no steps to reduce risk. Did not invest in a large number of policies as required to reduce risk. Initial Decision 24. These findings mischaracterize the evidence—including express authority to change business plan and asset mix—rely on unreliable evidence and ignore material other evidence.

The ALJ erroneously concluded that Respondents never told investors and potential investors that the strategy from the PPM changed. Initial Decision 28. These findings mischaracterize the evidence—including express authority to change business plan and asset mix—rely on unreliable evidence, ignore material other evidence, and mischaracterize the law and duties applicable to Respondents.

The ALJ erroneously concluded that Respondents did not advise auditors of impairment of the notes. Initial Decision 17. These findings mischaracterize the evidence, rely on unreliable evidence and ignore material other evidence.

The ALJ erroneously concluded that Jarkesy spoke highly of Am. West in a podcast that did not reflect the true condition of America West. Initial Decision 17. This finding mischaracterizes the evidence, relies on unreliable evidence and ignores material other evidence.

The ALJ erroneously concluded that Jarkesy sent an optimistic "Research Report" to investors in September 2010 and issued a press release regarding America West that did not reflect true financial condition of the company. Initial Decision 17. These findings mischaracterize the evidence, rely on unreliable evidence and ignore material other evidence.

The ALJ erroneously concluded that Alphametrix relied on Jarkesy for valuation of Galaxy because it was not publicly traded. Initial Decision 18. This finding mischaracterizes the evidence, relies on unreliable evidence and ignores material other evidence.

The ALJ erroneously concluded that from 2009 – 2011 Jarkesy valued shares wildly. Initial Decision 18. This finding mischaracterizes the evidence—including material corporate events affecting price—relies on unreliable evidence and ignores material other evidence.

The ALJ erroneously concluded that changes in price did not coordinate with events occurring inside Galaxy. Initial Decision 18. This finding mischaracterizes the evidence, relies on unreliable evidence and ignores material other evidence.

The ALJ erroneously concluded that together Jarkesy and Belesis exerted control over Galaxy. Initial Decision 18. This finding mischaracterizes the evidence, relies on unreliable evidence and ignores material other evidence.

The ALJ erroneously concluded that Fund I sold 300,000 shares of Radiant to Fund II in Aug. 2010 with a cost of $0.23 per share. Respondents increased the valuation of those shares the same month to $1.00 per share causing Fund I's unrealized profits to rise. Initial Decision 19. These findings mischaracterize the evidence, rely on unreliable evidence and ignore material other evidence.

The ALJ erroneously concluded that in December 2010 Radiant stock traded for the first time in 15 months at $4.00 per share coinciding with a marketing campaign. Initial Decision 19. This finding mischaracterizes the evidence, relies on unreliable evidence and ignores material other evidence.

The ALJ erroneously concluded that Jarkesy valued certain warrants in Radiant at $6.92 though they were previously valued at $0.12 four months earlier. Initial Decision 19.

This finding mischaracterizes the evidence, relies on unreliable evidence and ignores material other evidence.

The ALJ erroneously concluded that Jarkesy sent stock certificates of Radiant to certain fund investors on October 23, 2014 with a letter stating the Radiant shares were valued at least $2.00 per share. The closing price on Yahoo! Was $1.04 on Yahoo! Finance with no activity from October 24, 20134 through January 2, 2014. Initial Decision 20. These findings mischaracterize the evidence, rely on unreliable evidence and ignore material other evidence.

The ALJ erroneously concluded that Jarkesy initiated a promotional campaign in the fourth quarter of 2010 for America West stock. This caused the stock price to go up to $1.95 per share in December 2010. Subsequently on the financial statements, Jarkesy valued the stock at $1.95 per share. Initial Decision 20. These findings mischaracterize the evidence, rely on unreliable evidence and ignore material other evidence.

The ALJ erroneously concluded that Jarkesy initiated a promotional campaign for Radiant as well resulting in the share price going up to $4.00 per share in December 2010, resulting in very large gains reported on the year-end financial statements of the Funds. Initial Decision 20. This finding mischaracterizes the evidence, relies on unreliable evidence and ignores material other evidence.

The ALJ erroneously concluded that Fund I capped the aggregate capital commitments in any 1 company at 5%. Initial Decision 21. This finding mischaracterizes the evidence, relies on unreliable evidence and ignores material other evidence.

The ALJ erroneously concluded that marketing materials repeated the 5% limitation. Initial Decision 21. This finding mischaracterizes the evidence, relies on unreliable evidence and ignores material other evidence.

The ALJ erroneously concluded that Fund I did not meet the cap in 2007, 2008, 2009, or 2010. Initial Decision 21. This finding mischaracterizes the evidence, relies on unreliable evidence and ignores material other evidence.

The ALJ erroneously concluded that Belesis' input into decisions concerning portfolio companies and receipt of fees from such companies directly affected investors and losses. Initial Decision 29. This finding mischaracterizes the evidence, relies on unreliable evidence and ignores material other evidence.

All of these erroneous factual findings constitute prejudicial error and led to the erroneous legal findings.

(c) Erroneous Legal Findings

The ALJ erroneously concluded that Respondents violated the antifraud provisions in Section 17(a) of the Securities Act of 1933 and Section 10(b) of the Exchange Act of 1934 and Rule 10b-5 thereunder, and aided and abetted violations by the Funds of the same statutes. Initial Decision 24, 28, 29. There is insufficient evidence to support this conclusion, the findings of fact supporting this conclusion mischaracterize the evidence, and the ALJ ignored substantial evidence that contradicts this conclusion.

The ALJ erroneously concluded that Respondents violated the antifraud provisions in Sections 206(1), (2) and (4) of the Investment Advisors Act of 1940 and Rule 206(4)-8 thereunder, and aided and abetted violations by the Funds of the same statutes. Initial Decision 24, 28, 29. There is insufficient evidence to support these findings, the findings of fact supporting this conclusion mischaracterize the evidence, and the ALJ ignored substantial contrary evidence in the record.

The ALJ erroneously concluded that Respondents argue that the representations were not false when made and that the PPM gave JTCM discretion to change the investment strategy of the Fund. Yet Respondents never informed investors and potential investors of such changes. Initial Decision 28. These findings mischaracterize the evidence, mischaracterize the duties imposed upon Respondents, ignore substantial contrary evidence in the record, and are a misapplication of the law.

The ALJ erroneously concluded that Respondents may not rely upon advice of counsel as a defense because Respondents dis not claim that they consulted counsel before undertaking the actions. Initial Decision 28. There is insufficient evidence to support these findings and the ALJ ignores substantial contrary evidence in the record.

The ALJ erroneously concluded that Respondents misrepresented or failed to disclose the true relationship between Respondents and the settled co-respondents, and that such misrepresentation or omission was material. Initial Decision 29. There is insufficient evidence to support these findings, and the ALJ ignores substantial contrary evidence in the record.

The ALJ's finding of *scienter* is erroneous in that there is insufficient evidence to show that Respondents knew the representations in the offering materials to be false at the time they were made—or that they were false at all at the time they were made—and the ALJ erroneously concluded that Respondents had a duty to correct prior statements, but offers no legal support for this conclusion. Initial Decision 11.

The ALJ purported to address all of Respondents' constitutional claims by reciting case law supporting the ALJ's conclusion that the claims have no merit. Initial Decision 2-7. These findings are wholly improper in light of the following: 1) SEC APs do not permit counter claims, 2) the ALJ denied Respondents' request for issuance of subpoenas to obtain evidence to support their constitutional claims, 3) the ALJ failed to follow SEC procedures established to protect Respondents' constitutional rights, 4) the ALJ excluded evidence that supports Respondents' constitutional claims, thereby preventing review of the evidence, and 5) SEC ALJs do not have authority, procedural authority, training or expertise to deny constitutional claims asserted by Respondents.

X. The ALJ Erred in Imposing Remedies Against Respondents that are Unsupported, Disproportionate, and Contrary to Public Policy.

In light of the numerous defects to this AP, the sanctions ordered by the ALJ are: a) unsupported by the evidence, b) disproportionate in light of the allegations against and sanctions

levied on the settled co-respondents and in other similar cases, and c) contrary to public policy. All of the sanctions should be reversed.

The ALJ erred in ordering joint-and-several liability for Respondents for the following reasons: 1) there is no statutory authority for the imposition of disgorgement on joint-and-several liability in SEC administrative proceedings, 2) it was not alleged in the OIP, so Respondents were not on notice, 3) no evidence was presented at the hearing that JTCM is the alter ego of Jarkesy, nor was any other evidence presented to support piercing the corporate veil. Accordingly, there is no authority or basis for ordering joint-and-several liability. The case cited by the ALJ does not support the award of joint-and-several liability under an alter-ego theory.

The disgorgement amount is not supported by evidence in the record. As discussed above, Jarkesy received ***no profit*** from his participating in the venture, and actually lost money, like the other investors. As to JTCM, the ALJ appears to conflate revenue and profit for purposes of determining a disgorgement figure. The Funds and JTCM were not fraudulent enterprises, and a gross revenue figure is not a proper determination of disgorgement.

The lifetime securities industry bar is not in the public interest, nor is it necessary to serve as a deterrent. Jarkesy testified that he has no intention to manage any funds or to serve as an investment advisor in the future. While the fact that Respondents were not registered securities professionals—nor were they required to be—is not a barrier to a collateral securities industry bar, it should be. This is especially true given that the settled co-respondents were registered and had a fiduciary duty to the investors in the Funds—all of whom were also their clients. The lifetime bars recommended by the ALJ are out of proportion to the sanctions imposed on the settled co-respondents. The officer-and-director bar is also unwarranted. The conduct alleged in the OIP alleges no misconduct by Jarkesy in the role of an officer or director of a public

company. Accordingly, to bar him is not in the public interest, nor is it necessary to serve as a deterrent from future instances of the conduct alleged in the OIP.

Moreover, the sanctions ordered against Respondents are disproportionate compared to the sanctions levied upon settled co-respondents and compared to other cases. According to the OIP, the evidence adduced at the hearing, and the findings in the Initial Decision, JTF—a registered broker-dealer—and Belesis—a registered representative—played prominent roles in the transactions involving the Funds, including serving as placement agent offering and selling investments in the Funds, executing securities transactions for the Funds and serving as investment bank to certain of the companies in which the Fund had invested. According to the ALJ's findings, JTF's representatives made misrepresentation in connection with offering and selling investments in the Funds. Moreover, JTF and Belesis made five (5) times more money than Respondents allegedly made. In spite of these significant facts, JTF and Belesis received:

- 1 year securities-industry suspension;
- disgorgement and penalty of 17% of the total $6 million they received; and
- a lesser charge to a non-scienter fraud statute (which is supposedly contrary to Division policy).

For roughly equal conduct, Respondents received:

- Lifetime securities-industry bar (even though neither was required to register);
- Lifetime officer-and-director bar (even though no violations were alleged as officer or director of a public company);
- disgorgement and penalty of 135% of the almost 1.3 million they allegedly received;
- violations of all statutes charged in OIP; and
- cease-and-desist order.

By any standard, the sanctions to Respondents are inconsistent and inequitable.

CONCLUSION

This proceeding is void due to prejudgment by the Commission and the appearance of bias demonstrated by the Commission. This proceeding has violated—and continues to

violate—Respondents' constitutional rights to due process, equal protection, jury trial and in violation of the constitutional separation of powers. Moreover, numerous material facts alleged in the OIP have been disproven, other factual findings issued by the ALJ in the Initial Decision were not alleged, and numerous factual findings are not supported by credible evidence. The erroneous findings of fact serve as the basis for the conclusions of law that Respondents have committed violations of the securities laws, which conclusions of law are also erroneous. Finally, the recommended sanctions are not supported by the evidence, not permitted under the law, are unconstitutional, are grossly out of proportion to the sanctions imposed on the settled co-respondents and compared to other similar cases, and are contrary to public policy. This proceeding is fatally flawed and should be dismissed with prejudice and with no imposition of sanctions to Respondents.

Respectfully Submitted,

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Counsel for John Thomas Capital Management Group d/b/a Patriot28 LLC and George Jarkesy, Jr.

[redacted]

[redacted]

Exhibit A

SIMILARLY SITUATED DEFENDANTS
CHARGED BY SEC

Lead Defendant	SEC Link	File Date	Violations Alleged	Forum
Velten, Brian K. Civ. Act. No. 1:13-cv-23477	1	09-27-13	**§ 17(a) '33** **§ 10(b) '34** **§ 206(1), (2) '40**	S.D. Fla
Kirkland, Stephen Civ. Act. No. 1:13-cv-3150	2	09-23-13	**§ 10(b) '34** **§ 206(1), (2) '40**	N.D. Ga.
Hansen, Randal Kent Civ. Act. No. 13-cv-01403	3	03-01-13	**§ 17(a) '33** **§ 10(b)**, 15(a) **'34** **§ 206(1), (2), (4) '40**	S.D.N.Y.
Ng, Walter Civ. Act. No. C-13 0895	4	02-28-13	**§ 17(a) '33** **§ 10(b) '34** **§ 206(1), (2) '40**	N.D. Cal.
New Stream Capital, LLC Civ. Act. No. 3:13-cv-264	5	02-26-13	**§ 17(a) '33** **§ 10(b) '34** **§ 206(1), (2), (4) '40**	D. Conn.
Thomas, Delsa U. Civ. Act. No. 3:13-cv-00739	6	02-15-13	**§ 17(a) '33** **§ 10(b) '34** § 203A, **206(1), (2), (4) '40**	N.D. Tex.
Yorkville Advisors Civ. Act. No. 12-cv-7728	7	10-17-12	**§ 17(a) '33** **§ 10(b) '34** **§ 206(1), (2), (4) '40**	S.D.N.Y.
Deer Hill Financial Group Civ. Act. No. 12-01317	8	09-13-12	**§ 17(a) '33** **§ 10(b)**, 15(a) **'34** **§ 206(1), (2) '40**	D. Conn.
Gomez, Jorge Civ. Act. No. 1:12-cv-21962	9	05-29-12	**§ 10(b)**, 15(a) **'34** **§ 206(1), (2) '40**	S.D. Fla.

Legend:
Bold statutory sections in Violations Alleged column are identical to charges against Plaintiffs.
'33: Securities Act of 1933
'34: Securities Exchange Act of 1934
'40: Investment Advisers Act of 1940

1. (Velton)
   www.sec.gov/litigation/litreleases/2013/lr22821.htm

2. (Kirkland)
   www.sec.gov/litigation/litreleases/2013/lr22808.htm

3. (Hansen)
   www.sec.gov/litigation/litreleases/2013/lr22631.htm

4. (Ng)
   www.sec.gov/litigation/litreleases/2013/lr22628.htm

5. (New Stream Capital)
   www.sec.gov/litigation/litreleases/2013/lr22625.htm

6. (Thomas)
   www.sec.gov/litigation/litreleases/2013/lr22618.htm

7. (Yorkville)
   www.sec.gov/litigation/litreleases/2012/lr22510.htm

8. (Deer Hill Financial Group)
   www.sec.gov/litigation/litreleases/2012/lr22479.htm

9. (Gomez)
   www.sec.gov/litigation/litreleases/2012/lr22376.htm

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January 13, 2015

VIA HAND DELIVERY
Mr. Brent J. Fields, Secretary
Securities and Exchange Commission
100F Street, NE
Washington, DC 20549-1090
Facsimile 202.772.9324

RE: *John Thomas Capital Management Group LLC d/b/a Patriot28 LLC, et al.,*
File No. 3-15255

Respondents' Opening Brief

Dear Mr. Fields:

As counsel for respondents George R. Jarkesy, Jr. and Patriot28, LLC, pursuant to the Commission's Order Granting Review and Scheduling Briefs, dated December 11, 2014, I submit Respondents' Opening Brief in the above-captioned matter. Any questions concerning this matter can be directed to me at the contact information above.

Respectfully submitted,

Karen Cook