No. 22-1241

In the Supreme Court of the United States

JOCELYN M. MURPHY, MICHAEL S. MURPHY, AND RICHARD C. GOUNAUD,

Petitioners,

v.

SECURITIES AND EXCHANGE COMMISSION,

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

PETITIONERS' REPLY BRIEF IN SUPPORT OF PETITION FOR A WRIT OF CERTIORARI

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ARGUMENT

I. THE UNDISPUTED "VARIATION AMONG INDIVIDUAL AWARDS" IN SEC PENALTY CASES IS A RECURRING ISSUE OF NATIONAL ECONOMIC IMPORTANCE WARRANTING THE COURT'S REVIEW

SEC does not deny the widespread inconsistency and unpredictability surrounding its penalty awards in the hundreds of enforcement cases it files every year in both federal courts and its own administrative tribunal. SEC quibbles with Petitioners' characterization of the prevailing state as "chaos"—preferring the euphemism "variation among individual awards"—but it makes no effort to pretend the multiplicity of penalty-calculation approaches and disparate outcomes can be easily explained, harmonized, or justified. Opp. 20.

The Petition cited a multitude of SEC penalty-calculation methodologies used throughout the lower courts. Pet. 15–17. App. 30a–32a, 50a. SEC apparently approves of all of them. Opp. 20. In SEC's view, inconsistency and unpredictability are laudable features of its enforcement program because they give unelected agency officials and judges virtually limitless "discretion[,]" Opp. 13, 15, 19, 21, and "flexibility[,]" *id.* at 3, 18 (quoting S. Rep. No. 337, 101st Cong., 2d Sess. 10, 11 (1990)), to wait until the final stage of a case before revealing whether the penalty will be a few thousand dollars or hundreds of thousands or even millions. Over time, this has made the statutory penalty caps purposeless, while transferring to SEC and the courts the job of legislating the operative penalty caps (if any).

SEC likewise does not deny the enormous settlement leverage it derives from the prevailing penalty environment. *See Brief of Amici Curiae Securities Scholars and Former SEC Officials*. In just a single day last month, SEC reportedly extracted more than $200 million in administrative penalty settlements, none of which required judicial review. *See* DAVE MICHAELS, *SEC Brings in $218 Million in a Day but Still Faces Shutdown*, THE WALL STREET JOURNAL (Sept. 29, 2023) (last visited Oct. 10, 2023) https://www.wsj.com/finance/regulation/secs-whatsapp-fines-spread-further-across-wall-street-f1f097ea. SEC did not publicly explain its formula for calculating the penalty in any of those cases.

SEC likewise does not deny that its complaint pled a *singular* violation against each Petitioner for failing to register as a broker, along with a *singular* fraud violation against Petitioner Jocelyn Murphy.[1] That was a deliberate tactical choice by SEC. While a complaint need not include "detailed factual allegations regarding remedies[,]" Opp. 16, how a plaintiff pleads the violations should be highly relevant in determining the number of violations for penalty purposes and fair notice, and a plaintiff (especially a government prosecutor) ought not be permitted to plead and litigate a singular-violation theory only to switch gears at the remedies stage and seek potentially limitless penalties for numerous violations.

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[1] Ms. Murphy was also charged with violating a rule promulgated by the Municipal Securities Rulemaking Board, but SEC later abandoned that charge. Neither of the other Petitioners was charged with fraud or even negligence.

SEC wrongly contends that holding it to its singular-violation pleading means "someone who engages in a single trade as an unregistered broker, or who makes a single fraudulent misrepresentation in connection with a securities transaction, is subject to the same maximum penalty as someone who engages in such misconduct dozens (or thousands) of times." *Id*. at 18. Faced with those two hypothetical cases, courts would retain discretion to penalize the more culpable defendant up to the statutory maximum while imposing a lower fine (or none at all) on the one-time offender. This flexibility exists alongside SEC's own prosecutorial discretion to demand a penalty lower than the statutory cap (or to decline prosecution) against the more benign offender or to plead its case against a more culpable defendant with greater specificity by alleging multiple discrete violations.

SEC disputes that the decision below conflicts with the D.C. Circuit's decision in *Rapoport v. SEC,* 682 F.3d 98 (D.C. Cir. 2012), but that conflict is obvious. Each case involved failure to register as a broker. Each case imposed a penalty exceeding the nominal statutory cap by arbitrarily multiplying the cap by a random unit of time (here measured in months; there measured in years). Here, the Ninth Circuit upheld that multiplier as "reasonable" under the relevant statute, App. 31a, whereas *Rapoport* condemned it as an "inaccurate" and "faulty" approach that "do[es] not follow the formula set by the statute," 682 F.3d at 107–108.

Any minor differences between the two cases serve only to accentuate the circuit split—and the broader pan-circuit chaos—rather than reduce it. For example, the relevant statute in *Rapoport* authorized

penalties for "each act or omission" rather than for each violation, 682 F.3d at 101–02, thus at least arguably allowing SEC to slice a violation into component pieces. Even that language, however, was insufficient to convince the D.C. Circuit to affirm the per-unit-of-time multiplication method. Similarly, because *Rapoport* involved review of an administrative penalty, the court applied "extraordinarily deferential review," 682 F.3d at 107, yet still set the penalty aside.

Moreover, because the registration failure in *Rapoport* was intentional or reckless (unlike Petitioners' strict-liability failures), his statutory maximum per violation was approximately $60,000 (compared to the approximately $7,500 cap here). *Id*. at 102. Yet because SEC applied a per-*year* multiplier (rather than the per-*month* multiplier used here), the $315,000 penalty in *Rapaport* was just barely higher than Petitioner Gounaud's $309,000 penalty here, and more than $100,000 *lower* than Petitioner Sean Murphy's $419,000 penalty here—even though neither Gounaud nor Murphy was accused of acting intentionally or recklessly.

And what later happened in *Rapoport* makes the contrast between these two penalty outcomes almost surreal. As SEC notes, the D.C. Circuit remanded *Rapoport* so the agency could reconsider and better explain its penalty calculation. 682 F.3d at 108. But SEC never provided that explanation. Instead, it opaquely dropped the penalty from $315,000 to $39,000 in a settlement order issued several months later. *In re CentreInvest, Inc.*, SEC Exchange Act Rel. No. 68764 (Jan. 30, 2013).

SEC also dismisses Petitioners' comparison of the penalty provision at issue here and the one at issue in

Rapoport as "statutory apples to statutory oranges." Opp. 17 (quoting *SEC v. Fowler*, 6 F.4th 255, 256, cert. denied, 142 S. Ct. 590 (2021)). But SEC is the one comparing dissimilar provisions. SEC asks the Court to compare the "each violation" language of the applicable statute here (Securities Exchange Act of 1934 § 21(d)(3)(B), 15 U.S.C. § 78u(d)(3)(B)) with the language of a *non-parallel* subsection of the penalty statute at issue in *Rapoport* (Securities Exchange Act of 1934 § 21B(a)(1), 15 U.S.C. § 78u-2(a)(1)). Opp. 17.[2] But the only useful comparison is between the *parallel* provisions of these two sections—*i.e.*, § 21(d)(3)(B) versus § 21B(b). That side-by-side comparison—of parallel provisions enacted in two immediately contiguous sections of the same legislation in 1990, *see* Securities Enforcement Remedies and Penny Stock Reform Act of 1990 §§ 201–202, 104 Stat. 931, 936–37—leaves no doubt that Congress used more *limiting* language in the applicable provision here (with emphasis added below):

[2] Petitioners cannot fathom the logic behind SEC's insistence that the aiding-and-abetting language in the non-parallel provision is relevant here. That language applies only in SEC in-house administrative cases, and in any event, SEC did not charge Petitioners with aiding and abetting.

§ 21(d)(3)(B) **(applied here)**	**§ 21B(b)** **(applied in *Rapoport*)**
"The amount of the penalty shall be determined by the court in light of the facts and circumstances. *For each violation*, the amount of the penalty *shall not exceed the greater of* (I) $5,000 for a natural person or $50,000 for any other person, or (II) the gross amount of pecuniary gain to such defendant as a result of the violation."	"The maximum amount of penalty *for each act or omission* described in subsection (a) of this section *shall be* $5,000 for a natural person or $50,000 for any other person."

Given this contrast, SEC cannot plausibly contend that Congress intended to allow penalties to be imposed for "each act or omission" under either provision. The Ninth Circuit's agreement with that contention was therefore fundamentally mistaken.

This Court's recent decision in *Bittner v. United States*, 143 S. Ct. 713 (2023), also undermines the decision below rather than bolstering it, as SEC contends. Opp. 14. In *Bittner*, the petitioners violated a statutory requirement to file annual tax reports, so it was entirely logical to count each inaccurate annual report as a separate violation. There was no suggestion that mere passage of time, untethered to any required periodic filing obligation, is enough to

use a random unit of time as a proxy for a new violation. Petitioners here allegedly had a *singular* obligation to register with SEC as brokers, not an annual (much less monthly) obligation to re-register.[3] Equally important, *Bittner* rejected the government's position that each individual bank account erroneously omitted from an annual report constituted a separate violation. 143 S. Ct. at 719–21. Of particular relevance here, *Bittner* contrasted the language of the applicable penalty provision with that of nearby penalty provisions within the same statute. *Id*. at 720 ("When Congress includes particular language in one section of a statute but omits it from a neighbor, we normally understand that difference in language to convey a difference in meaning").

SEC's substantive response to Petitioner's Excessive Fines claim rests entirely on the premise that the penalties were "substantially lower" than the applicable statutory caps. Opp. 20 (quoting App. 34a–36a). In SEC's and the Ninth Circuit's apparent view, the district court had the "flexibility" and "discretion" to impose penalties anywhere from $1 to more than $10 million against each of the Petitioners (approximately $7,500 for each of their "thousands" of transactions and approximately $75,000 for each of 21 emails sent by Petitioner Jocelyn Murphy).[4] SEC

[3] Although some brokers are required to make periodic filings with SEC, *see, e.g.*, 17 C.F.R. § 240.17a-5(a), SEC did not charge Petitioners with violating these requirements.

[4] By logical extension, SEC and the Ninth Circuit presumably would approve of an even higher theoretical penalty ceiling achieved through even more ingenious counting of violations—such as counting each *day* of non-registration or each written or oral communication made while unregistered.

does not dispute that if Petitioners are correct that their penalties vastly exceeded the applicable statutory caps, they could also be excessive under the Eighth Amendment.

Both SEC and the Ninth Circuit vastly overstate the purported gravity of Petitioners' violations for Eighth Amendment purposes. The claim that Petitioners caused "systemic harm" by "undermin[ing] the retail bond market" and an "important system of government oversight in the securities industry" is, to say the least, vastly exaggerated. Opp. 20 (alteration in original) (quoting App. 35a). By that logic, the same could be said of virtually every failure to register as a broker and every inaccuracy in securities-related emails. Petitioners were relatively minor individual traders in a vast municipal securities market saturated with financial institutions both large and small; they traded in their own brokerage accounts held at large SEC-registered brokerage firms; and they had no reason to predict that SEC would claim they needed to register as brokers. *See generally Brief of Amici Curiae Investor Choice Advocates Network*.

Equally relevant is that Petitioners were first-time offenders, their profits were so modest that SEC eschewed the statutory alternative penalty calculation tied to "the gross amount of pecuniary gain," *see* 15 U.S.C. § 78u(d)(3)(B); App. 47a–48a, they caused no investor harm or loss, and their registration violations were strict-liability offenses involving neither scienter nor negligence. If these offenses threatened such systemic risk to the retail bond market and the entire machinery of market oversight as to warrant outsized penalties, it is difficult to conjure any securities-law violation that

would not. Penalties routinely imposed for comparable offenses present a more accurate assessment of the relative gravity of these offenses—or lack thereof. *Cf. SEC v. Pac. W. Capital Group*, No. 15-cv-02563-DDP-ASx, 2023 U.S. Dist. LEXIS 143888 at *2–5 (C.D. Cal. Aug. 10, 2023) ($15,000 total penalty for *both* failing to register as broker *and* participating in unregistered securities offerings); *SEC v. Barry*, No. 15-cv-02563-DDP-ASx, 2023 U.S. Dist. LEXIS 120200 at *17–19 (C.D. Cal. Jul. 12, 2023) (similar); *SEC v. VerdeGroup Inv. Partners, Inc.*, No. 21-cv-07663-SB-ADS, 2022 U.S. Dist. LEXIS 127852, at *17–18 (C.D. Cal. 2022) ($5,000 penalty); *SEC v. Core Performance Mgmt., LLC*, No. 18-cv-81081-BB (S.D. Fla. Aug. 16, 2018) (Judgment against James O'Neil) (approving $7,500 penalty settlement); *SEC v. RMR Asset Mgmt. Co.*, No. 18-cv-01895 (S.D. Cal. Aug. 17, 2018) (Judgment against David Luttbeg) (approving $7,500 penalty settlement). SEC cites no comparable strict-liability case—whether settled or contested—with a penalty for failing to register as a broker anywhere close to the penalties imposed here.

SEC's suggestion that the Court ignore these dramatically lower penalties because they resulted from settlements should be rejected. First, the above-cited cases (and others not cited) include both settled and contested outcomes, so SEC is wrong to suggest that statutory caps apply only in settled cases. More importantly, the decision to contest governmental charges of wrongdoing, by itself, cannot justify geometrically higher penalties. It is one thing to impose a penalty *lower than* the statutory cap to *reward* a settling litigant, but something wholly different—and odious—to contrive arbitrary

gimmicks to *punish* non-settlers with penalties that vastly *exceed* a statutory cap.

II. THE NINTH CIRCUIT'S UNPRECEDENTED EXPANSION OF WHO MUST REGISTER WITH SEC AS A BROKER WARRANTS THE COURT'S REVIEW

SEC's defense of the Ninth Circuit's unprecedented expansion of the definition of "broker" hinges primarily on an ultra-literal reading of the statutory definition. But this Court has repeatedly eschewed such literal readings of statutory definitions—particularly in securities law, starting with narrowing the statutory definition of "security" itself—where a literal reading would sweep in actors or financial instruments that do not need SEC regulation or were plainly never intended by Congress to be swept in. *See*, *e.g.*, *Reves v. Ernst & Young*, 494 U.S. 56, 63 (1990) (not all "notes" are securities); *Marine Bank v. Weaver*, 455 U.S. 551, 556–59 (1982) (not all certificates of deposit are securities).

When the Exchange Act was enacted in 1934, "broker" was generally understood to mean someone who earned commissions to execute trades for customers. *See Broker*, WEBSTER'S NEW INTERNATIONAL DICTIONARY (2d ed. 1934). The statutory definition—"any person engaged in the business of effecting transactions in securities for the account of others[,]" 15 U.S.C. § 78c(a)(4)(a)—reflects that contemporaneous, understanding. Based on that understanding, SEC has created an elaborate set of regulations designed to protect investors who open and trade through securities accounts at registered brokerage firms like Merrill Lynch. Petitioners here

availed themselves of those protections by opening trading accounts at several SEC-registered firms so that those firms could then execute transactions for their accounts. It is undisputed that Petitioners never received any commissions and never executed any trades—the two main roles of a "broker" as that term was understood in 1934.

The Ninth Circuit nevertheless held that Petitioners were not just customers but brokers themselves, primarily because a third party provided funds for their brokerage accounts and shared in the trading profits and losses. Neither SEC nor any court had ever before read the term broker so broadly, as implicitly conceded by SEC. The Ninth Circuit's expansive new definition threatens to sweep within the definition of broker many other types of customers—at least those doing business within the circuit—who engage in no traditional brokerage activities and would likely be "surprise[d]" to learn that they must incur the substantial regulatory costs and burdens associated with SEC registration and oversight. *See Brief of Amici Curiae Investor Choice Advocates Network* at 8–14.

The Court should grant certiorari and establish reasonable limits on who must register with SEC as a broker.

III. THE NINTH CIRCUIT'S PERMISSIVE ALLOWANCE OF SUMMARY JUDGMENT TO ABRIDGE JURY TRIAL RIGHTS WARRANTS REVIEW

This Court has established strict guardrails for summary judgment to prevent courts from depriving litigants of their right to a jury trial. Those guardrails are especially important when government

prosecutors seek through summary judgment to impose quasi-criminal penalties and to brand defendants as wrongdoers.[5] Here, the lower courts plowed through those guardrails both to establish liability and to impose massive punitive sanctions against Petitioners.

SEC contends the evidence submitted by Petitioners was either immaterial or conclusory. Opp. 25–27. But Petitioners' sworn declarations provided detailed factual averments, not merely legal conclusions, and SEC cannot deny that the courts below ignored one of this Court's most important summary judgment guardrails: that all inferences be drawn in favor of the non-moving party. *Anderson v. Liberty Lobby*, 477 U.S. 242, 255 (1986). Here, all inferences were drawn *against* Petitioners. Nor has SEC denied that the lower courts made credibility findings against the Petitioners in determining both liability and penalties.

Given the degree to which the Ninth Circuit disregarded this Court's summary judgment guardrails, this case presents an excellent opportunity for the Court to reinforce the sanctity of jury trial rights when disputed facts are fairly contested, particularly where government prosecutors seek to use the procedural shortcut of summary judgment to impose quasi-criminal penalties.

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[5] This Court has never decided whether the Seventh Amendment (or Sixth) precludes summary judgment in favor of a governmental prosecutor in a quasi-criminal case (particularly if premised on a mere preponderance of evidence), a procedural shortcut that would be unthinkable in a conventional criminal case.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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