ORAL ARGUMENT NOT YET SCHEDULED

14-1194 (consolidated with 14-5242)

In the United States Court of Appeals for the District of Columbia Circuit

NEW YORK REPUBLICAN STATE COMMITTEE and TENNESSEE REPUBLICAN PARTY, *et al.*,
Petitioners-Appellants,

v.

SECURITIES AND EXCHANGE COMMISSION,
Respondent-Appellee.

On Appeal from the United States District Court for the District of Columbia (No. 14-01345, Judge Beryl A. Howell)

CORRECTED BRIEF *AMICUS CURIAE* OF FINANCIAL SERVICES INSTITUTE, INC. IN SUPPORT OF APPELLANTS

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December 30, 2014

Corporate Disclosure Statement Pursuant to Circuit Rule 26.1

Pursuant to FED. R. APP. P. 26.1, the undersigned counsel for the *amicus curiae* certify that the Financial Services Institute, Inc. has no parent company and further certify that no publicly-held company owns more than 10% of the Financial Services Institute, Inc. The Financial Services Institute, Inc. is a not-for-profit corporation organized under the laws of Georgia. All Parties have consented to the filing of this brief.

Table of Contents

Page

Corporate Disclosure Certificate Pursuant to Circuit Rule 26.1 i

Table of Contents ii

Table of Authorities iv

Glossary...vi

Interest of the Financial Services Institute, Inc., *Amicus Curiae* 1

ARGUMENT 3

I. AS APPLIED, THE RULE RESTRICTS THE INDEPENDENT BROKER-DEALER COMMUNITY BEYOND WHAT IS NECESSARY TO ACHIEVE THE RULE'S PROPHYLACTIC GOALS. 3

A. FSI's Member Firms Are Composed of Independent Contractors Who Operate Their Own Businesses, Which Differentiates Them From Other Market Participants. 3

B. The Potential for the Campaign Contribution Abuse Targeted by Rule 206(4)-5 Is Nonexistent in FSI's IBD Firms. 4

C. The IBD Community Has Had To Adopt an Overbroad Construction of the Rule in Order To Prevent Inadvertent and Inconsequential Technical Violations of the Rule. 6

II. INTERPRETING A RULE OF GENERAL APPLICABILITY AS AN ADJUDICATIVE ORDER IS ERROR, AND PERMITS THE SEC TO AVOID JUDICIAL REVIEW. 7

A. To the Extent That *Investment Company Institute* Controls, It Should Be Limited or Reconsidered. 7

1. The experience of FSI and its members conclusively demonstrates that material developments relevant to an Administrative Procedure Act challenge will develop after the 60-day petition period. 10

2. Congress did not intend to foreclose review of administrative rules based upon these later developments. 10

B. The District Court's Ruling Effectively Permits the SEC To Block Judicial Review of Its Regulations. 13

C. The First Amendment Requires Swift Judicial Review of Laws and Regulations That Infringe Upon Political Speech and Association, Regardless of When Those Burdens Become Clear. 14

CONCLUSION 16

Certificates of Compliance 18

Table of Authorities

Page(s)

CASES

Buckley v. Valeo, 424 U.S. 1 (1976) 9

Citizens United v. FEC, 558 U.S. 310 (2010) 15, 16

Conn. Nat'l Bank v. Germain, 503 U.S. 249 (1992) 12

Davis v. FEC, 554 U.S. 724 (2008) 15

**FEC v. Wisconsin Right to Life, Inc.*, 551 U.S. 449 (2007) 15

**Investment Company Institute v. Board of Governors of the Federal Reserve System*, 551 F.2d 1270 (D.C. Cir. 1977) 7, 8, 9, 10

McCutcheon v. Fed. Election Comm'n, 134 S. Ct. 1434 (2014) 15

Raton Gas Transmission Co. v. FERC, 852 F.2d 612 (D.C. Cir. 1988) 9

SEC v. Chenery Corp., 332 U.S. 194 (1947) 9, 11

Virginia v. Black, 539 U.S. 113 (2003) 15

**Watts v. SEC*, 482 F.3d 501 (D.C. Cir. 2007) 8

RULES & STATUTES

5 U.S.C. § 553(e) 13

17 C.F.R. 201.192(a) 13

17 C.F.R. 201.192(b)(1) 13

OTHER AUTHORITIES

ADMINISTRATIVE PROCEDURE ACT: LEGISLATIVE HISTORY 79TH CONGRESS, 1944-46 (DOC. NO. 248) 12

D.C. Circuit L.R.4(a)(1)(A) 11

Authorities upon which we chiefly rely are marked with asterisks.

Joe Mont, Political Spending Disclosures Not on SEC's Agenda in 2014,
COMPLIANCE WEEK (Dec. 2, 2013)..14

Securities and Exchange Commission Rule 206(4)-5 .... 2, 3, 4, 5, 6, 7, 9, 10, 16

Glossary

APA	Administrative Procedure Act
FSI	Financial Services Institute, Inc.
SEC	Securities and Exchange Commission
IBD	Independent Broker-Dealer

Interest of Financial Services Institute, Inc., *Amicus Curiae*

The Financial Services Institute ("FSI") was founded in 2004 with a clear mission: to ensure that all individuals have access to competent and affordable financial advice, products, and services delivered by a growing network of independent financial advisors and independent financial services firms. FSI's members are independent broker-dealers ("IBDs") and their registered representatives who operate as independent contractors. FSI has over 100 broker-dealer member firms with more than 138,000 affiliated registered representatives who serve more than 14 million American households. FSI also has more than 35,000 independent "financial advisor" members. The term "financial advisor" is used generically to refer to independent contractors of a broker-dealer. Such independent contractors are registered as registered representatives, investment advisory representatives or may be dually-registered as both registered representatives and investment advisory representatives.

In the United States, there are approximately 167,000 independent financial advisors, which account for approximately 64.5 percent of all producing registered representatives.

While a traditional brokerage firm may provide comprehensive financial services through its broker-dealer operations, an IBD often has a broad network of registered representatives who are not employees, but rather independent

contractors. These financial advisers are self-employed independent contractors, rather than employees of the IBD firms. Independent financial advisers are entrepreneurial business owners who typically have strong ties, visibility, and individual name recognition within their communities and client base. Thus, these financial advisers have a strong incentive to make the long term achievement of their clients' investment objectives their primary goal. Financial advisors are registered as investment advisor representatives and many operate independent investment advisory practices that provide advisory services to individuals and also to pension funds and other government retirement plans. Financial advisors also provide advisory services through their IBD firms which are registered as investment advisers.

As a result, FSI member firms are subject to Rule 206(4)-5. As a practical matter, as shown below, IBDs have had to establish overly broad prohibitions in order to achieve compliance with the Rule. This creates a burden upon such entities—many of them small businesses themselves—in a context where there is little to no risk of pay-to-play corruption.

ARGUMENT

I. AS APPLIED, THE RULE RESTRICTS THE INDEPENDENT BROKER-DEALER COMMUNITY BEYOND WHAT IS NECESSARY TO ACHIEVE THE RULE'S PROPHYLACTIC GOALS.

A. FSI's Member Firms Are Composed of Independent Contractors Who Operate Their Own Businesses, Which Differentiates Them From Other Market Participants.

IBDs typically maintain dual registrations: registration as a broker dealers and registration as investment advisers with the SEC. They are called "independent" because the individuals who utilize those registrations to deliver financial services to clients are not employees of the firm but rather are independent contractors with whom the firm has a business to business relationship. Advisory services may be provided under the brand of the IBD firm or may also be provided through the financial advisor's separately registered independent investment advisory firm.

By contrast, the archetypal, non-IBD firm (i) employs its own registered representatives and investment adviser representatives (ii) who go to market under their employer's brand, and (iii) who provide brokerage and investment advisory services only under the centralized control of the parent entity.

Rule 206(4)-5 (the "Rule") is not tailored to the manner in which advisory services are provided by financial advisors in the IBD model. Instead of recognizing that advisory services can be offered under one roof but through

various independent adviser entities, the Rule contemplates that advisory services offered through a single IBD firm are necessarily inter-related. In this regard, we note that the Rule provides that a contribution by either the adviser itself or one of the adviser's "covered associates" may trigger the Rule's two year ban on providing advisory services. The Rule defines "covered associate" to include "any employee who solicits a government entity for the investment adviser and any person who supervises, directly or indirectly, such employee." In other contexts, the staff of the SEC has interpreted the term "employee" to include independent contractors. As a result, the Rule treats independent contractors as employees and therefore as "covered associates" to the extent that they solicit a government entity for the investment adviser.

B. The Potential for the Campaign Contribution Abuse Targeted by Rule 206(4)-5 Is Nonexistent in FSI's IBD Firms.

Rule 206(4)-5 was intended to prevent a registered investment adviser from improperly influencing a governmental entity's choice of pension fund investment managers through the concerted use of campaign contributions made by that firm's personnel to public officials in a position to influence that choice. Preventing improper influence over the choice of pension fund managers by governmental entities is a laudable goal, and FSI and its members support it.

However, the rule does not account for the manifest differences in the way IBD firms and non-IBD firms provide advisory services. In the IBD firm, the

independence of one representative from another means that their investment management activities are unconnected to one another and their political contributions are also unconnected and uncoordinated. However, the Rule, as firms have been forced to apply it, treats all of these businesses as being housed under one roof.

It is entirely appropriate that the Rule prevent a particular financial advisor from using political contributions to induce a public officer to retain that financial advisor's investment managers. But the Rule forces IBD firms to prevent *all* financial advisors of the IBD – no matter how independent they may be from one another – from making contributions to a public official whose governmental entity is served by *some other* financial advisor of that IBD.

As a practical matter, IBDs have been forced to treat all financial advisers as covered associates instead of making case-by-case determinations regarding whether a financial adviser is covered by virtue of their seeking to solicit a governmental entity. This has resulted in IBDs imposing broad prohibitions on financial advisor contributions in excess of the *de minimis* limits set forth in the rule and also prohibiting contributions to PACs.

C. The IBD Community Has Had To Adopt an Overbroad Construction of the Rule in Order To Prevent Inadvertent and Inconsequential Technical Violations of the Rule.

IBD firms have had to apply the Rule in an overbroad way. To illustrate, a single IBD firm might have three financial advisors that are affiliated with three separate independent investment adviser representatives called Alpha Advisors, Beta Advisors and Charlie Advisors in, say, Ohio. Alpha Advisors might have the contract to manage the public employee pension funds for the state of Ohio. Its "covered persons" (general partners, managing members or officers) would properly be restricted from making contributions to Ohio politicians in a position to influence the state's choice of investment managers.

But the Rule in effect forces IBD firms to treat all of its financial advisors as covered and to connect the activities of the three advisory firms and prohibit the officers of Beta Advisors and Charlie Advisors from making political contributions to those Ohio politicians *even though their firms do no business with Ohio and any advisory business they do is separate from Alpha Advisors.*

As written, therefore, the Rule has an unintentionally overbroad *in terrorem* application to IBD firms. They have adopted restrictions on their independent representatives to prevent facial violations of the Rule, even though the practical problem sought to be resolved by the Rule is entirely absent.

FSI files this brief as *amicus curiae* in order to bring to the Court's attention the impact that the Rule has on IBD firms and their affiliated financial advisors.

II. INTERPRETING A RULE OF GENERAL APPLICABILITY AS AN ADJUDICATIVE ORDER IS ERROR, AND PERMITS THE SEC TO AVOID JUDICIAL REVIEW.

The Parties and the district court agree that Rule 206(4)-5 is, befitting its name, a rule of general applicability and not an adjudicative order. Op. at 11 ("The Commission does not dispute that the Challenged Rule is in fact a 'rule' and not an 'order'"). Nevertheless, the district court felt constrained by this Court's precedents to convert that rule into an adjudicative order, and consequently found that it lacked subject matter jurisdiction. This was error, and ought to be reversed.

A. To the Extent That *Investment Company Institute* Controls, It Should Be Limited or Reconsidered.

The district court's ruling relied upon this Court's opinion in *Investment Company Institute v. Board of Governors of the Federal Reserve System*. 551 F.2d 1270 (D.C. Cir. 1977) (*"ICI")*. The district court determined that "under [*ICI*]…the term order encompasses rules." Op. at 11 (punctuation altered, citation omitted).

As a preliminary matter, it is not obvious that *ICI* controls this case. The plaintiff in *ICI* was a repeat player before the Board of Governors, and—before attempting to challenge the underlying rulemaking—failed to appeal two adjudicative orders levied against it by the Board. 551 U.S. at 1274-1275. The *ICI* Court was not denying the Investment Company Institute its day in federal court. It

was merely noting that the Institute had failed to attack the rules it opposed when the appropriate opportunity, in the form of an adjudicative proceeding, had previously presented itself. *ICI*, 551 F.2d at 1278 ("The rules in question here…could therefore have been challenged through a timely petition in this court under section 9 of the Bank Holding Act"). The circumstances here are distinguishable. Plaintiffs—as well as FSI—only determined the scope of the new rule's burdens on associational liberty after several years' experience, and without having waived appeal of any SEC order.

Indeed, the district court suggested that *ICI* may well be limited to the circumstances of that case, since "the D.C. Circuit has since instructed courts to 'look to the Administrative Procedure Act…when an agency's direct-review statute [does] not define 'order.'" Op. at 16 (quoting *Watts v. SEC*, 482 F.3d 501, 505 (D.C. Cir. 2007)). The district court, however, declined to apply *Watts*, largely because it "did not cite to or discuss the holding of *Investment Company Institute*." Op. at 17. Of course, another reading may be that *ICI*, a case interpreting section 9 of the Bank Holding Act, should not apply to a case involving review of SEC action.

But even if this Court determines that *ICI* applies broadly, that is not determinative. This Court has determined "that there may be review of agency action outside the statutory review period in extreme cases involving gross

violations of statutory or constitutional mandates, or denial of an adequate opportunity to test the regulation in court." *Raton Gas Transmission Co. v. FERC*, 852 F.2d 612, 615 (D.C. Cir. 1988). Given that Rule 206(4)-5 dramatically narrows the right to contribute to candidates for public office, which the Supreme Court has found to be a "basic constitutional freedom…[that] lies at the foundation of a free society," and the district court felt compelled to impose burdens, discussed in more detail below, upon obtaining "an adequate opportunity to test the regulation in court," it would be appropriate to apply the *Raton Gas Transmission* exception in this instance. *Buckley v. Valeo*, 424 U.S. 1, 24 (1976).

But even if this Court decides that *ICI* controls, that case ought to be limited or reconsidered. The district court's opinion provides a number of reasons why interpreting an agency rule as an agency order creates absurd results. Op. 13-20. For decades, in the administrative law context, federal courts have deferred to the procedural process—rule or order—as determined by the agency. *SEC v. Chenery Corp.*, 332 U.S. 194, 203 (1947) ("And the choice made between proceeding by general rule or by individual, *ad hoc* litigation is one that lies primarily in the informed discretion of the administrative agency"). The SEC has always treated Rule 206(4)-5 as a rule, not an order, and it would be inappropriate to infringe upon the agency's own understanding of its internal procedures. *ICI* notwithstanding, a rule ought to be reviewed as a rule.

After three years of compliance with Rule 206(4)-5, FSI and its members have come to understand the burdens of that compliance, and this new information ought to be heard in a judicial proceeding. Furthermore, it would be astounding if Congress intended, in passing the Administrative Procedure Act, to place agency decision making outside of the scope of normal Article III review.

1. **The experience of FSI and its members conclusively demonstrates that material developments relevant to an Administrative Procedure Act challenge will develop after the 60-day petition period.**

FSI and its members have now spent three years struggling with the burdens imposed by Rule 206(4)-5. *E.g. supra* at 6-7. The same may be said of Plaintiffs. None of this information was presented to the Commission when it considered promulgating the Rule, and it was therefore not considered by the agency. These circumstances ought to place this case outside of the scope of *ICI,* because the complaint against the agency's rule cannot "be resolved on the basis of the administrative record." *ICI*, 551 F.2d at 1278. These facts counsel in favor of finding subject matter jurisdiction, and suggest that *ICI* is inapplicable here.

2. **Congress did not intend to foreclose review of administrative rules based upon these later developments.**

The district court noted that its holding goes against the grain of the Administrative Procedure Act. Op. at 14 ("Indeed, the distinction between rules and orders is the dichotomy upon which the most significant portions of the APA

are based") (citation and quotation marks omitted). The SEC suggests that Congress simultaneously created judicial review of agency rules while intending for rules to be treated as orders falling outside the scope of that judicial review. This is an improbable reading of Congress's intention in passing the Administrative Procedure Act.

The 60-day clock for appeals for orders rests in good sense. Orders typically apply only to a specific party and those similarly situated. That party has immediate notification of the order, and is best situated to file an appeal. It has intimate knowledge of the relevant record, and plainly has a vested interest in the outcome. In other words, orders closely resemble judicial decisions. By extension, the appellate process—including a strict jurisdictional limit for timely appeals—appropriately reflects the process in a civil lawsuit. *See e.g.* D.C. Circuit L.R.4(a)(1)(A) ("In a civil case…the notice of appeal required…must be filed with the district clerk within 30 days").

But rules of general applicability operate as statutes, not court orders. *SEC v. Chenery Corp.*, 332 U.S. 202 (describing the SEC's "ability to make new law prospectively through the exercise of its rule-making power" as "quasi-legislative"). To obtain subject matter jurisdiction to challenge a campaign finance law, such as the contribution limits of the Federal Election Campaign Act or the Bipartisan Campaign Reform Act, a plaintiff does not have to demonstrate

exhaustion by petitioning Congress to first amend the law. Such a requirement would deny plaintiffs the right to immediate and meaningful review of unconstitutional statutes.

Such concerns in part motivated the passage of the APA. That statute was the product of over a decade of serious efforts to grapple with the explosion of independent governing bodies after the New Deal. ADMINISTRATIVE PROCEDURE ACT: LEGISLATIVE HISTORY 79TH CONGRESS, 1944-46 (DOC. NO. 248), Forward ("[I]t has been through a most rigorous and lengthy sieve of consideration by the Congress"). Judicial review is a vital backstop to the reality of unelected agencies that exercise powers normally reserved to elected officials. In that vein, the APA was especially designed to "lighten[] the burden of those on whom the law may impinge." *Id*.

It would be remarkable if Congress intended that agency rules must be interpreted as orders, with the attendant 60-day clock on jurisdiction. This would be an especially odd reading given the clear demarcation between the two processes in the APA. "Courts must presume that a legislature says in a statute what it means and means in a statute what it says there. When the words of a statute are unambiguous, this first canon is also the last: 'judicial inquiry is complete.'" *Conn. Nat'l Bank v. Germain*, 503 U.S. 249, 253-254 (1992) (quoting *Rubin v. United States*, 449 U.S. 424, 430 (1981)).

B. The District Court's Ruling Effectively Permits the SEC To Block Judicial Review of Its Regulations.

The district court maintained that its ruling does not impose any significant burden on the plaintiffs. The court noted that plaintiffs may simply "petition the SEC to amend the rule. Should the SEC reject the proposed amendment, a new sixty-day clock would start within which period the party could file for review in the appropriate Court of Appeals." Op. at 16. *Amicus* disagrees.

It is true that the APA permits any "interested person the right to petition for the issuance, amendment, or repeal of a rule." 5 U.S.C. § 553(e). But it does not require the agency to act with dispatch. The SEC's own regulations regarding rulemaking petitions simply note that those "desiring the issuance, amendment[,] or repeal of a rule of general application may file a petition therefore with the Secretary." 17 C.F.R. 201.192(a). But the Secretary is only required to "acknowledge, in writing, receipt of the petition and refer it to the appropriate division or office for consideration and recommendation." *Id*. Those recommendations are than sent to the full SEC, which may take "such action as the Commission deems appropriate." *Id*. If the Commission decides to go forward with a rulemaking, it must give public notice of the proposed rulemaking and "afford [interested persons] the opportunity to participate in such proceeding." 17 C.F.R. 201.192(b)(1).

Noticeably absent from the SEC's regulations is any time limit on such action. Under the statute, the Commission could hold a rulemaking petition in abeyance for quite some time. For example, the Commission has been slow in responding to a rulemaking petition, File No. 4-637, from 2011. This petition sought "to require public companies to disclose to shareholders the use of corporate resources for political activities." Despite significant public interest, the SEC has not opened a rulemaking. Joe Mont, Political Spending Disclosures Not on SEC's Agenda in 2014, COMPLIANCE WEEK (Dec. 2, 2013).[1]

Nevertheless, the district court's opinion has now granted the SEC wide berth to constructively evade judicial review of its regulations for significant periods of time. Given the sensitive nature of securities regulation, it would be remarkable if the agency was permitted to simply evade judicial review of its rules by allowing a process to slowly and interminably drag on. This cannot be squared with any fair conception of due process especially where, as here, fundamental constitutional rights are implicated.

C. The First Amendment Requires Swift Judicial Review of Laws and Regulations That Infringe Upon Political Speech and Association, Regardless of When Those Burdens Become Clear.

Seven years ago, the Supreme Court stated that obstacles to judicial review of laws with First Amendment implications can themselves "constitute[] a severe

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[1] *Available at*: http://www.complianceweek.com/blogs/the-filing-cabinet/political-spending-disclosures-not-on-secs-agenda-in-2014.

burden on political speech." *FEC v. Wisconsin Right to Life, Inc.*, 551 U.S. 449, 468 n. 5 (2007) ("*WRTL II*"). The circumstances in that case differed somewhat from those here—the *WRTL II* plaintiff received its day in court and had its case decided on the merits. But the district court had ordered extensive discovery which, in his controlling opinion, Chief Justice Roberts determined was excessive—and itself a First Amendment harm.

The Chief Justice went on to find that "the proper standard" for resolving First Amendment challenges must "allow parties to resolve disputes quickly without chilling speech through the threat of burdensome litigation." *WRTL II*, 551 U.S. at 469. Delay is impermissible, as it inevitably means that the plaintiff and other would-be speakers will be forced to comply with the law for a longer length of time—which is an ever-present problem in campaign finance cases.[2] *See Citizens United v. FEC*, 558 U.S. 310, 334 (2010) ("Today, Citizens United finally learns, two years after the fact, whether it could have spoken during the 2008 Presidential primary—long after the opportunity to persuade primary voters has passed"). Worse yet, procedural burdens might, in and of themselves, chill potential plaintiffs from filing suits challenging unconstitutional laws. *See Virginia*

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[2] Indeed, this is such a recurring problem in the campaign finance context that many cases must be decided under the "capable of repetition, yet evading review" exception to mootness. *Davis v. FEC*, 554 U.S. 724 (2008); *WRTL II*, 551 U.S. 449 (2007); *Citizens United*, 558 U.S. 310 (2010); *McCutcheon v. FEC*, 134 S. Ct. 1434 (2014).

v. Black, 539 U.S. 113, 119 (2003) ("Many persons, rather than take the considerable burden (and sometimes risk) of vindicating their rights through case-by-case litigation, will choose simply to abstain from protected speech").

"A [contributor's] ability to engage in" First Amendment activity "is stifled if the [contributor] must first commence a protracted lawsuit." *Citizens United*, 558 U.S. at 334. The harm is compounded if a plaintiff must take the additional step of first filing a petition for rulemaking. As this Court should clarify, such an additional delay is unlikely to have been what Congress had in mind when it subjected agency rulemakings to judicial oversight.

CONCLUSION

After three years' experience, FSI and its members have come to an intimate understanding of the burdens imposed by compliance with Rule 206(4)-5. In particular, IBD firms have had to impose broad restrictions on their financial advisors to prevent facial violations of the Rule, even though the practical problem sought to be resolved by the Rule are largely absent. Given that Rule 206(4)-5 is a rule of general applicability and not an adjudicative order, the district court's failure to find subject matter jurisdiction was in error and ought to be reversed.

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Certificates of Compliance

1. FRAP Rule 29(a), Circuit Rule 29(b). All parties consent to the filing of this amicus curiae brief.

2. Circuit Rule 29(d). Counsel for FSI hereby certifies that a separate brief is necessary because FSI's independent broker-dealer members and their independent contractor registered representatives and FSI's independent financial advisors would be uniquely damaged by the SEC's interpretation of SIPA.

3. FRAP Rule 29(c)(5). FSI's attorneys authored this brief without assistance, and no person other than FSI paid the expenses of its preparation.

4. FRAP 32(a)(7)(B); Circuit Rule 32(a)(2)(C). This brief complies with the type-volume limitations of FED. R. APP. P. 32(a)(7)(B) because this brief contains 3,525 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

5. FRAP 32(a). This brief complies with the typeface requirements of FED. R. APP. P. 32(a)(5) and the type-style requirements of FED. R. APP. P. 32(a)(6) because this brief has been prepared in a proportionally spaced typeface using Word 2010 in 14 point Times New Roman Type.

Dated: December 30, 2014

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that a true and correct copy of the foregoing Corrected Brief Amicus Curiae of Financial Services Institute, Inc. in support of the District Court's Order was served on December 30, 2014 upon the following individuals via ECF:

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