No. 24-1899

In the United States Court of Appeals For the Ninth Circuit

THOMAS JOSEPH POWELL, et al.,

Petitioners

v.

UNITED STATES SECURITIES AND EXCHANGE COMMISSION,

Respondent

On Petition for Review from the United States Securities and Exchange Commission No. 4-733

BRIEF OF AMICUS CURIAE INSTITUTE FOR FREE SPEECH IN SUPPORT OF PETITIONERS AND REVERSAL

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DISCLOSURE STATEMENT

Counsel for amicus curiae Institute for Free Speech, Nathan J. Ristuccia, certifies that IFS has no parent company, subsidiary, or affiliate, and that no publicly held company owns more than 10 percent of its stock.

Dated: June 24, 2024

/s/ *Nathan J. Ristuccia*
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INTERESTS OF AMICUS CURIAE[1]

The Institute for Free Speech is a nonpartisan, nonprofit organization dedicated to the protection of the First Amendment rights of speech, assembly, petition, and press. In addition to scholarly and educational work, the Institute represents individuals and civil society organizations in litigation securing their First Amendment liberties. Challenging unreasonable and discriminatory burdens on public advocacy is a core aspect of the Institute's mission.

This case matters to the Institute because it implicates the government's ability to distort the marketplace of ideas by shielding itself from criticism. The SEC's systematic silencing of former defendants impoverishes public debate. And it prevents the Institute from hearing petitioners' experiences with the SEC's enforcement regime and drawing on that information in the Institute's scholarship, commentary, and legislative testimony in defense of First Amendment rights.

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[1] No counsel for a party authored this brief in whole or in part, nor did any person or entity, other than amicus curiae or its counsel, financially contribute to preparing or submitting this brief. All parties have consented to the Institute filing this amicus brief.

INTRODUCTION AND SUMMARY OF ARGUMENT

For more than fifty years, the Securities and Exchange Commission (SEC) has used the threat of debilitatingly expensive litigation to coerce defendants into accepting a lifetime ban on speech. The SEC's Gag Rule commands that, once defendants have settled, they can never publicly challenge—or even permit others to undermine—the truth of the SEC's factual allegations, even if those allegations are indisputably false.

The SEC's Gag Rule is a ban not just on speech but a ban on *true political* speech. It imposes an eternal, viewpoint-discriminatory prior restraint on speech critical of the SEC's enforcement regime. For a country with "a profound national commitment to the principle that debate on public issues should be uninhibited, robust, and wide-open, and that it may well include vehement, caustic, and sometimes unpleasantly sharp attacks on government and public officials," the unconstitutionality of this policy is clear. *New York Times Co. v. Sullivan*, 376 U.S. 254, 270 (1964). Nonetheless, the SEC refuses to initiate a rulemaking to amend its Gag Rule.

The SEC justifies its policy by claiming that defendants consent to their gag orders and thus voluntarily waive their First Amendment rights in exchange for the benefits. But the SEC categorically refuses to negotiate any settlement without a gag order. *SEC v. Moraes*, No. 22-cv-8343 (RA), 2022 U.S. Dist. LEXIS 196811 (S.D.N.Y. Oct. 28, 2022). Instead, the SEC unconstitutionally conditions settlement on defendants surrendering their rights. *See Koontz v. St. Johns River Water Mgmt. Dist.*, 570 U.S. 595, 604 (2013).

The SEC's Gag Rule harms the public interest by shielding the agency from public accountability, denying vital information from the legislative and executive branches, barring defendants' right to petition for redress of grievances, and contracting away the rights of third parties and the press to hear what former defendants wish to communicate. Because the Gag Rule operates to keep necessary information and advocacy from the public and the political branches of government, a political solution to this abuse is in practice impossible. The judiciary alone can intervene. This Court should grant the petition and require the SEC to initiate a rulemaking to amend its policy.

ARGUMENT

I. THE SEC COERCES DEFENDANTS INTO SURRENDERING THEIR FREEDOM OF SPEECH IN EXCHANGE FOR SETTLEMENT

A. The SEC's Gag Rule discriminates on the basis of viewpoint against speech critical of the agency

The SEC's Gag Rule coerces defendants into accepting a lifelong, viewpoint-discriminatory prior restraint on their speech as a condition of avoiding debilitatingly expensive litigation.

It is axiomatic that the government may not "regulat[e] speech when the specific motivating ideology or the opinion or perspective of the speaker is the rationale for the restriction." *Rosenberger v. Rector and Visitors of the Univ. of Va.*, 515 U.S. 819, 829 (1995). Viewpoint discrimination is "an egregious form of content discrimination," in which "the government targets not [just] subject matter, but particular views taken by speakers on a subject." *Id.* Although content-based speech restrictions can be valid if they satisfy strict scrutiny, "restrictions based on viewpoint are prohibited." *Pleasant Grove City v. Summum*, 555 U.S. 460, 469 (2009) (citations omitted).

The Gag Rule is "textbook" viewpoint discrimination. *Moraes*, 2022 U.S. Dist. LEXIS 196811, at *11. The Rule prohibits anyone who has settled a lawsuit or enforcement action with the SEC from "creating . . .

an impression that . . . the conduct alleged did not, in fact, occur" by "denying the allegations in the complaint or order for proceedings" or by indirectly "permitting to be created" the impression that the allegations are false. 17 C.F.R. § 202.5(e).

Everlasting silence is not enough. Because the SEC "believes that a refusal to admit the allegations is equivalent to a denial," the Rule compels speech. Whenever a defendant refuses to admit the SEC's charges, the defendant must also publicly "state[] that he neither admits nor denies the allegations," *id.*, or the settlement is breached and the SEC may reopen its enforcement, *see SEC v. Novinger*, 40 F.4th 297, 301 (5th Cir. 2022); Dkt. 1 (SEC's denial of petition) at 10.

Under the Gag Rule, therefore, if a defendant "wishes to speak, she must either speak as the State demands or face sanctions for expressing her own beliefs" which is "an impermissible abridgment of the First Amendment's right to speak freely." *303 Creative LLC v. Elenis*, 143 S. Ct. 2298, 2313 (2023). Moreover, "the coercive elimination of dissenting ideas" about the SEC's enforcement regime "constitutes [the agency's] very purpose" in applying its rule. *Id.* The SEC established the Gag Rule in 1972 to insulate the agency from public criticism. Before 1972,

former defendants often publicly insisted that they were innocent and had settled merely to avoid the costs of litigation. *See SEC v. Vitesse Semiconductor Corp.*, 771 F. Supp. 2d 304, 308 (S.D.N.Y. 2011) (presenting the policy's history). The SEC feared these future denials would "undermine the agency's integrity" and reputation with the public, making it seem that the agency "was acting arbitrarily, or worse unlawfully." David Rosenfeld, *Admissions in SEC Enforcement Cases: The Revolution That Wasn't*, 103 IOWA L. REV. 113, 118-19 (2017); *see also* Dkt. 1 (SEC's denial of petition) at 12 (warning that denials "could undermine confidence in the Commission's enforcement program").

Of course, the policy allows former defendants to praise the SEC in public or confess their alleged wrongdoing. *Moraes*, 2022 U.S. Dist. LEXIS 196811, at *11. Indeed, former defendants can even deny the truth of the SEC's allegations, if they do so in "private statements." SEC Opp'n to Mot. for Relief from J. 23, *SEC v. Allaire*, No. 03-cv-4087 (S.D.N.Y. 2019), Dkt. 31 at 25; *see also* Dkt. 1 (SEC's denial of petition) at 10 (noting that only "public statements" breach the gag order). But defendants cannot "petition appropriate government bodies to secure changes in the Commission's enforcement practices," "speak, write,

and/or publish" publicly about the SEC's enforcement action, or "critique the Commission more generally," if these petitions, public communications, or critiques create the impression that the SEC's allegations are false. SEC Opp'n, *SEC v. Allaire*, *supra* at 25 (internal quotations omitted). And the SEC forbids such communications even when the SEC's allegations were indisputably false. *Moraes*, 2022 U.S. Dist. LEXIS 196811, at *1-2.

The SEC cannot ban speech critical of its enforcement practices, while permitting and even compelling supportive speech. Protecting the agency's reputation is not a compelling interest justifying suppressing any speech—let alone, the true political speech, which the Gag Rule targets. *See N.Y. Times*, 376 U.S. at 272-73; *see also L.G. Balfour Co. v. FTC*, 442 F.2d 1, 24 (7th Cir. 1971) (agency's order "may not prohibit the telling of a true statement even if that representation perpetuates" unfair trade practice). For "political speech is core First Amendment speech, critical to the functioning of our democratic system," which "enjoys special status" and "rests on the highest rung of the hierarchy of First Amendment values." *Long Beach Area Peace Network v. City of Long Beach*, 574 F.3d 1011, 1021 (9th Cir. 2009) (cleaned up).

The SEC's Gag Rule unconstitutionally discriminates against political speech on the basis of both content and viewpoint.

B. Gag orders under the SEC's policy operate as a prior restraint on political speech

The SEC's Gag Rule also constitutes a classic prior restraint, for it forces defendants to agree to "an administrative or judicial order that forbids certain communications issued before those communications occur." *Greater L.A. Agency on Deafness, Inc. v. CNN, Inc.*, No. 12-15807, 2014 U.S. App. LEXIS 2492, at *37 (9th Cir. Feb. 5, 2014).

"[P]rior restraints on speech and publication are the most serious and the least tolerable infringement on First Amendment rights," because they are "by definition . . . an immediate and irreversible sanction" that "freezes" speech. *Neb. Press Ass'n v. Stuart*, 427 U.S. 539, 559 (1976). Prior restraints "carry a heavy presumption of invalidity." *Long Beach*, 574 F.3d at 1023 (internal quotation marks omitted). They are unconstitutional unless "imposed only for a specified brief period" with "narrow, objective, and definite standards to guide" discretion. *Nat'l Sec. Letters v. Sessions*, 33 F.4th 1058, 1071 (9th Cir. 2022).

The SEC enforces its gag orders through the threat of prosecution, fines, or even criminal contempt. *See Cato Inst. v. SEC*, 4 F.4th 91, 95

(2021). The SEC has unbridled discretion to decide what speech violates the order by "permitting to be created[] an impression" that the SEC's allegations are false, 17 C.F.R. § 202.5(e), and the gag is not for a brief period but eternal. "A more effective prior restraint is hard to imagine." *Novinger*, 40 F.4th at 308 (Jones, J, concurring).

C. The SEC's Gag Rule unconstitutionally conditions settlement on the surrender of First Amendment rights

By refusing to negotiate any consent agreements that lack a gag order, the SEC imposes an unconstitutional condition on settlement.

"[T]he unconstitutional conditions doctrine . . . vindicates the Constitution's enumerated rights by preventing the government from coercing people into giving them up." *Koontz*, 570 U.S. at 604. Even when the government "is under no obligation to provide . . . a particular benefit," it cannot make "conferral of the benefit . . . conditioned on the surrender of a constitutional right . . . especially his interest in freedom of speech." *44 Liquormart v. Rhode Island*, 517 U.S. 484, 513 (1996) (citation and quotation marks omitted). "Where private speech is involved," the government's decision to grant or withhold benefits "cannot be aimed at the suppression of ideas thought inimical to the

Government's own interest." *Legal Servs. Corp. v. Velazquez*, 531 U.S. 533, 548-49 (2001).

"Before the government can require a citizen to surrender a constitutional right as part of a settlement or other contract, it must have a legitimate reason for including the waiver in the particular agreement." *Davies v. Grossmont Union High Sch. Dist.*, 930 F.2d 1390, 1399 (9th Cir. 1991). The government must prove "a close nexus—a tight fit—between the specific interest the government seeks to advance in the dispute underlying the litigation involved and the specific right waived." *Id*. There also must be clear and convincing evidence that the waiver was "knowing, intelligent, and voluntary." *SEC v. ACI Inv'rs Protective Ass'n*, No. 95-56644, 1996 U.S. App. LEXIS 27593, at *13 (9th Cir. Oct. 22, 1996); *see also Davies*, 930 F.2d at 1395.

This Court, for instance, held that plea agreements cannot condition probation on the defendant's agreeing not to publicly criticize a government official for five years—even though the speech in that case was "inflammatory," "discriminatory," and targeted at one person. *United States v. Richards*, 385 F. App'x 691, 693 (9th Cir. 2010). Other circuits have come to similar conclusions. *See, e.g., Overbey v. Mayor of*

Balt., 930 F.3d 215, 219 (4th Cir. 2019) (non-disparagement clause demanded as a condition of settlement void due to "strong public interests rooted in the First Amendment"); *G&V Lounge, Inc. v. Mich. Liquor Control Comm'n*, 23 F.3d 1071, 1077 (6th Cir. 1994) (contract unenforceable as "condition[s] Plaintiff's receipt of a benefit upon Plaintiff's waiver of its right to free expression").

Civil settlement agreements are unconstitutional if they lack a close nexus between the specific interest and the specific waiver. *See, e.g., Emmert Indus. Corp. v. City of Milwaukie*, 307 F. App'x 65, 67 (9th Cir. 2009) (litigation waiver "rationally related to the benefit conferred" as waiver "not a but-for dealbreaker" and focused on ending specific dispute about run-down house); *Lil' Man In The Boat, Inc. v. City & County of San Francisco*, No. 17-cv-00904-JST, 2017 WL 3129913, at *9–10 (N.D. Cal. July 24, 2017) (broad litigation waiver covering all future disputes fails close nexus test).

The SEC's Gag Rule lacks any close nexus between the SEC's interest in the litigation—protecting investors from securities violations—and the free speech rights of defendants. Indeed, the Gag Rule keeps information from investors and ensures that "the public will

never know whether the S.E.C.'s charges are true." *Vitesse*, 771 F. Supp. 2d at 309. Under the Gag Rule, both defendants who were genuinely guilty and those who settled to avoid litigation costs are treated the same and both can later emphasize that they never admitted charges—although the difference between these types of defendants matters greatly to investors. In fact, former defendants are allowed to deny the truth of the SEC's allegations to potential investors, as long as they do so in "private statements." SEC Opp'n, *SEC v. Allaire*, *supra* at 25; *see also* Dkt. 1 (SEC's denial of petition) at 10. Burnishing the agency's reputation, not protecting investors, is the purpose of the Gag Rule.

The rights waiver, moreover, is not "knowing, intelligent, and voluntary." The policy forbids defendants from merely *permitting* the creation of an *impression* that allegations are untrue, 17 C.F.R. § 202.5(e): vague language that "fails to provide people of ordinary intelligence a reasonable opportunity to understand what conduct it prohibits" and "authorizes or even encourages arbitrary and discriminatory enforcement." *Hill v. Colorado*, 530 U.S. 703, 732 (2000) (citation omitted).

Defendants cannot know exactly what speech they are waiving and such "uncertain meanings inevitably lead citizens to steer far wider of the unlawful zone than if the boundaries of the forbidden areas were clearly marked." *Grayned v. City of Rockford*, 408 U.S. 104, 108 (1972) (cleaned up). And, because the SEC refuses to negotiate consent agreements without a gag order, these agreements are not actually voluntary. "If you want to settle, SEC's policy says, 'Hold your tongue, and don't say anything truthful—ever'—or get bankrupted by having to continue litigating with the SEC." *Novinger*, 40 F.4th at 308 (Jones, J, concurring).

D. The Gag Rule impedes public accountability and reform of the SEC's enforcement regime

Even if protecting the SEC's reputation were a legitimate government interest justifying censorship, the Gag Rule fails to achieve its goal. By thwarting public accountability, the Gag Rule heightens criticism of the agency. Dkt. 1 (Commissioner Peirce's dissent) at 18 ("far from shoring up the Commission's integrity, the reliance on these no-denial conditions undermines it").

After the Global Financial Crisis of 2007-2008, for example, critics charged that the SEC colluded with the worst offenders and uses no-

deny settlements to cover this up. *See SEC v. Bank of Am. Corp.*, 653 F. Supp. 2d 507, 512 (S.D.N.Y. 2009) ("The proposed Consent Judgment in this case suggests a rather cynical relationship between the parties: the S.E.C. gets to claim that it is exposing wrongdoing . . . the Bank's management gets to claim that they have been coerced into an onerous settlement by overzealous regulators. And all this is done at the expense, not only of the shareholders, but also of the truth."); *see also* Rosenfeld, *supra* at 120-21, 176 (discussing "the perception that the SEC was acting collusively with defendants" due to "a complete lack of consistency and transparency in the use of the [no-deny] policy").

The Gag Rule does not refute false rumors of agency corruption; it merely prevents accountability by hindering journalists and academics from investigating the SEC's enforcement behavior and proposing evidence-based reforms. "Because of their dealings with the government," former defendants "are often in the best position to know what ails the agencies." *Bd. of Cnty. Comm'rs v. Umbehr*, 518 U.S. 668, 674 (1996) (cleaned up). They are "the members of [the] community most likely to have informed and definite opinions" on SEC enforcement, so "it is essential that they be able to speak out freely on

such questions without fear of retaliat[ion]." *Pickering v. Bd. of Educ.*, 391 U.S. 563, 572 (1968).

The SEC is already insulated from accountability, for its commissioners are "neither elected by the people nor meaningfully controlled (through the threat of removal) by someone who is." *Seila Law LLC v. CFPB*, 140 S. Ct. 2183, 2203 (2020). Uninhibited public debate, however, would check abuses and ensure public accountability. "Sunlight" is "the best of disinfectants," the most efficient "remedy for social and industrial diseases." *Buckley v. Valeo*, 424 U. S. 1, 67 (1976) (per curiam) (citation omitted). As long as the SEC continues to insist that it needs to silence its critics, the American people will increasingly suspect the agency has something to hide.

II. THE SEC'S GAG RULE UNCONSTITUTIONALLY RESTRAINTS THE RIGHT TO PETITION THE GOVERNMENT

By prohibiting all former defendants from denying allegations or permitting the impression that charges were false, the SEC eliminates defendants' right to petition the government for redress of grievances.

The right to petition is "integral to the democratic process" for it empowers "citizens to express their ideas, hopes, and concerns to their government and their elected representatives." *Borough of Duryea v.*

Guarnieri, 564 U.S. 379, 388 (2011). Although the freedoms to speak and petition often employ the same analysis, in some cases "the special concerns of the Petition Clause would provide a sound basis for a distinct analysis" that extends "further than the right to speak." *Id.* at 388-89. "Interpretation of the Petition Clause must be guided by the objectives and aspirations that underlie the right." *Id.* at 388. "The Petition Clause protects [petitioners] against retaliation for filing petitions" if "those petitions are addressed to the government in its capacity as their sovereign." *Id.* at 400 (Thomas, J., concurring in judgment) (cleaned up).

The SEC's consent agreements regularly exempt from the Gag Rule a defendant's testimonial obligations or right to take positions in legal proceedings in which the SEC is not a party. James Valvo, *The CFTC and SEC are Demanding Unconstitutional Speech Bans in their Settlement Agreements*, NOTICE & COMMENT: YALE J. REG. (Dec. 4, 2017), https://www.yalejreg.com/nc/the-cftc-and-sec-are-demanding-unconstitutional-speech-bans-in-their-settlement-agreements-by-james-valvo/ (collecting and analyzing agreements). The SEC recognizes, that is, that consent agreements cannot undermine the judicial system.

Yet these same agreements perpetually inhibit defendants' interactions with the legislative and executive branches. Former defendants cannot deny allegations or permit an impression of falsehood when they are lobbying legislators or agencies, commenting on proposed rules, speaking before Congressional hearing, submitting a petition to Congress, or communicating publicly in any other way with the first two branches of government. *See* SEC Opp'n, *SEC v. Allaire*, *supra* at 25. Former defendants can "petition appropriate government bodies to secure changes in the Commission's enforcement practices" and "critique the Commission more generally" as long as they do not "deny the allegations" while petitioning. *Id.* Put another way, defendants can petition the government as long as they never mention any grievances that need redressing.

Of course, the SEC allows former defendants to praise the SEC or admit the Commission's allegations before the legislature or executive. *Moraes*, 2022 U.S. Dist. LEXIS 196811. Only criticizing the SEC and seeking redress of grievances defendants have with the agency's enforcement are forbidden. The Gag Rule retaliates against the exact conduct that the First Amendment protects.

The SEC's no-denial policy is remarkably similar to perhaps the most famous violation of freedom of petition in American history: the House of Representative's gag resolutions against abolitionism. In 1836, pro-slavery legislators imposed a procedural rule preventing any petition about slavery from being printed, read, acted on, or referred to in the House. Kathy Hessler, *Early Efforts to Suppress Protest: Unwanted Abolitionist Speech*, 7 B.U. PUB. INT. L.J. 185, 210-15 (1998). Anti-slavery congressmen condemned these gag resolutions as unconstitutional abridgments of freedom of petition and, in 1844, convinced the House to end the rule. Gregory A. Mark, *The Vestigial Constitution: The History and Significance of the Right to Petition*, 66 FORDHAM L. REV. 2153, 2216-26 (1998). Former president John Q. Adams, for instance, insisted that the resolutions "interfere[d] with the sacred right of petition." Hessler, *supra* at 211 n.173.

The SEC's Gag Rule operates much like these pro-slavery gag resolutions. It singles out a particular topic—the past SEC settlement—as off limits to government petitions. It prevents defendants from providing true information to the legislature and executive or calling into question the SEC's enforcement regime. Like pro-slavery

Southerners, the SEC is not content with just voting against reforms; it wants to stop abuses from ever being discussed. The gag rule frustrates the democratic process and the objectives and aspirations underlying the Petition Clause. *See Borough of Duryea*, 564 U.S. at 388-89.

III. THE SEC CANNOT AGREE WITH DEFENDANTS TO THE WAIVE THE RIGHTS OF THE PRESS AND OTHER THIRD PARTIES

The SEC's coercive gag orders, moreover, harm the public interest, by depriving third parties and the press of the information needed to report effectively on securities enforcement or advocate reforms.

"It is now well established that the Constitution protects the right to receive information and ideas." *Stanley v. Georgia*, 394 U.S. 557, 564 (1969). Because "it is the purpose of the First Amendment to preserve an uninhibited marketplace of ideas in which truth will ultimately prevail," the public possesses "the right to receive suitable access to social, political, esthetic, moral, and other ideas." *Kleindienst v. Mandel*, 408 U.S. 753, 762-63 (1972) (cleaned up) (collecting cases). "The right of citizens to inquire, to hear, to speak, and to use information to reach consensus is a precondition to enlightened self-government and a necessary means to protect it." *Citizens United v. Fed. Election Comm'n*, 558 U.S. 310, 339 (2010).

Gag orders and similar prior restraints on speech can violate the public's right to listen and the press' right to gather information. *See, e.g.*, *Thomas v. Collins*, 323 U.S. 516, 534 (1945) (overturning law requiring labor organizers to register before solicitating members as a violation of workers' right "to hear what he had to say"); *Crosby v. Bradstreet Co.*, 312 F.2d 483, 485 (2d Cir. 1963) (reversing consent order enforceable through contempt as "a prior restraint by the United States against the publication of facts which the community has a right to know"); *State ex rel. The Missoulian v. Mont. Twenty-First Judicial Dist. Court*, 933 P.2d 829, 842 (Mont. 1997) (gag order reviewed under "heightened scrutiny standard" to protect "the media's First Amendment rights as receivers of information").

This Court invalidated a prison policy stopping the delivery of mail containing material downloaded from the internet, as a violation of the inmates' "First Amendment right to receive information." *Clement v. Cal. Dep't of Corr.*, 364 F.3d 1148, 1151 (9th Cir. 2004). Even in a context with as high state interests as the prison system, this Court subjected the policy to heightened scrutiny and demanded that the state

"articulate a rational or logical connection between its policy and these interests." *Id.* at 1152.

The SEC cannot articulate a rational connection between its Gag Rule and any legitimate government interest. The agency's gag orders infringe on the rights of the press and other third parties to receive information about the SEC's enforcement regime. Even if the former defendants genuinely did "consent" to these gag orders, the agency and defendants cannot together agree to contract away the constitutional rights of third parties.

CONCLUSION

The Court should vacate the Commission's denial of the rulemaking petition, and remand with instructions for the SEC to engage in rulemaking to remove the Gag Rule from 17 C.F.R. § 202.5(e).

Dated: June 24, 2024

Respectfully submitted,

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UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

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Signature _/s/ *Nathan J. Ristuccia*_ **Date** _June 24, 2024__

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/s/ *Nathan J. Ristuccia*
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