UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

UNITED STATES SECURITIES AND EXCHANGE COMMISSION, **Plaintiff,** **v.** **MORNINGVIEW FINANCIAL, LLC and MILES M. RICCIO,** **Defendants, and** **JOSEPH M. RICCIO, JR.,** **Relief Defendant.**	**Case No.: 1:22-cv-08142-VM**

BRIEF OF ALTERNATIVE INVESTMENT MANAGEMENT ASSOCIATION, LTD., TRADING AND MARKETS PROJECT, INC., AND THE NATIONAL ASSOCIATION OF PRIVATE FUND MANAGERS AS AMICI CURIAE IN SUPPORT OF DEFENDANTS AND DISMISSAL

Anthony S. Barkow (N.Y. Bar #4745220)
Charles D. Riely (N.Y. Bar #4091609)
Jenner & Block LLP
1155 Avenue of the Americas
New York, NY 10036
(212) 891-1662
abarkow@jenner.com
criely@jenner.com

Gabriel K. Gillett (N.Y. Bar #5011705)
Counsel of Record
Jenner & Block LLP
353 North Clark Street
Chicago, IL 60654
(312) 840-7220
ggillett@jenner.com

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INTEREST OF AMICI CURIE[1]

The Alternative Investment Management Association, Ltd. ("AIMA") is the global representative of the alternative investment industry. AIMA's members collectively manage over $2 trillion in hedge fund assets and include some of the world's largest, most sophisticated investors.

Trading and Markets Project, Inc. is a non-partisan, non-profit organization dedicated to enhancing capital markets and ensuring the stability and competitiveness of the financial system.

The National Association of Private Fund Managers ("NAPFM") represents the legal and economic interests of investment advisers in the private fund management industry, which serve a diverse set of investors including pensions, endowments, and insurers.

Amici and their members have a strong interest in how courts and the Securities and Exchange Commission ("SEC" or "Commission") define the meaning of the term "dealer" under the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. § 78c(a)(5). Many members of amici—including investment advisers and managers of hedge funds and other investment vehicles—have long understood that they are not "dealers" under the Exchange Act based on the language of the statute, the underlying history and context, and years of guidance from the SEC. But in a handful of very recent cases, including this one, the SEC appears to be arguing for the first time for a much broader definition of the term "dealer" than courts have traditionally recognized. The SEC has even argued that *any* person that buys and sells securities as a business is a "dealer," regardless of whether they satisfy the statutory definition as it has historically been understood and applied. *See* Dkt. 23 ("SEC Opp.") at 1, 7, 17.

[1] As noted in the accompanying unopposed letter motion for leave, Defendants consent to the filing of this brief and the SEC does not oppose the filing of this brief if it is given 30 days to file a response. No party or party's counsel authored this brief in whole or in part or contributed money intended to fund preparing or submitting the brief, and no person other than amicus or its members or counsel contributed money intended to fund preparing or submitting the brief. *Cf.* Fed. R. App. P. 29.

As Defendants explain, the SEC is wrong to contend that these Defendants are dealers. Amici write separately to support Defendants' position on the law and to amplify why the SEC's arguments could have consequences beyond this case—including for markets and many market participants—and why the Court should take that into account in its ruling.

INTRODUCTION AND SUMMARY OF ARGUMENT

This case raises important issues of statutory interpretation because the SEC proposes breaking with nearly a century of precedent and reinterpreting the securities laws contrary to their long-understood meaning. The Exchange Act defines a "dealer" as "any person engaged in the business of buying and selling securities … for such person's own account," 15 U.S.C. § 78c(a)(5)(A), and includes an express exemption for persons buying and selling securities "not as a part of a regular business," *id.* § 78c(a)(5)(B). That language historically has been understood as limiting "dealer" status to a narrow category of entities that buy and sell securities to execute *customer* orders. Here, however, the SEC suggests that *anyone* who is "engaged in the business of buying and selling securities" for their own account may be a dealer. *See* SEC Opp. at 7, 17, 19. That reading contravenes the Exchange Act's text, conflicts with the long-settled understanding of its meaning, and contradicts the SEC's own prior guidance and holdings. The "dealer" definition was never intended to cast such a wide net. It was meant to be limited to those who transact in their own account with or for *customers* as part of a "regular business"—not to reach other market participants like investment advisers that transact on behalf of clients or funds or other institutional investors that transact for investment purposes.

The SEC's broad theory should be rejected. Sweeping consequences could result if the SEC could state a claim by alleging a business buying or selling securities is a "dealer"—regardless of whether the transactions were part of a "regular business" for executing customer orders, or the

presence of other factors the SEC and market participants have traditionally relied on. Under the SEC's view, almost any professional adviser or investor could arguably be deemed a dealer. This could obligate hedge funds, mutual funds, pension funds, insurance companies, family offices, banks, endowments, foundations, individual investors, and others to register as dealers, subject them to burdensome regulations that have no logical application to their business, and place them at risk of severe sanctions for engaging in ordinary investment activities that were never thought to require dealer registration. Adhering to the well-settled meaning of "dealer" the SEC and market participants have used for nearly ninety years—is textually and historically correct, and avoids ensnaring broad swaths of investors in a thicket of inappropriate and unnecessary regulation.

If the SEC wishes to prohibit the activity at issue in this case, it has ample tools available. It could ask Congress to amend the definition of "dealer." Perhaps it could issue a new rule or amend an existing one that fills perceived gaps, balances costs and benefits, and accounts for stakeholder input. (The SEC's current proposal to redefine "dealer" does not, which raises questions about its decision to pursue enforcement actions and rulemaking simultaneously.) But enforcement actions like this one, proceeding at the SEC's discretion, are not appropriate for upsetting the well-established meaning of "dealer." Whatever the vehicle, the SEC may not misconstrue the text, history, and settled understanding of the Exchange Act to target activity it may now dislike.

ARGUMENT

I. Registered Investment Advisers And Funds Are Operated And Regulated Differently From Dealers.

A. Registered Investment Advisers And Funds Seek Returns For Investors.

Investors today have a range of investments and investment vehicles available to achieve their financial goals. Many rely on the expertise of investment advisers, who are "paid for provid-

ing advice about securities to their clients." FINRA, *Investment Advisers*, https://tinyurl.com/2vch7fx8 (visited June 29, 2023).

Private investment funds are "usually structured as limited partnerships" to achieve "maximum separation of ownership and management," where "the general partner manages the fund (or several funds) for a fixed fee and a percentage of the [fund's] gross profits" and "[t]he limited partners are passive investors and generally take no part in management activities." *Goldstein v. SEC*, 451 F.3d 873, 876 (D.C. Cir. 2006); *see* AIMA, FAQs, https://tinyurl.com/34vwwur9 (visited June 29, 2023). In managing the fund, the general partner typically hires an adviser that may have discretion to invest and trade for the fund's own account. *See* FINRA, *supra*. Hedge funds, for example, can provide competitive, diversified, uncorrelated risk-adjusted returns, as well as downside protection and flexibility. *See* AIMA FAQs, *supra*; *Goldstein*, 451 F.3d at 876.

Investors can also utilize other investment vehicles, including private equity funds, registered investment companies, pension funds (public or private), and family offices. Collectively, their economic impact is substantial. In 2021, U.S. pension plans held over $27 trillion in assets. *See* Cong. Rsch. Serv., *U.S. Retirement Assets: Amount in Pensions and IRAs* (2022), https://tinyurl.com/4xt9yzeh. In 2022, mutual funds were owned by 115.3 million investors and 52.3% of U.S. households. Investment Co. Inst., Mutual Funds Are Key to Building Wealth for Majority of US Households (Oct. 31, 2022), https://www.ici.org/news-release/22-news-ownership.

Among instruments available to investors are convertible notes or bonds, which typically have periodic interest payments but also include "the option to convert [the security] into shares of the underlying company at a later date, often at a discounted rate." *See* Tim Stobierski, Harv. Bus. Sch. Online, *What is Arbitrage?* (July 20, 2021), https://tinyurl.com/5x263fba. Convertible bonds are attractive to companies looking to reduce their cost of capital and provide those with

low or no credit ratings with access to funding when they may lack other options. *See* Elizabeth Howcroft et al., Reuters, *RPT-Convertible Bond Issues Surge in Coronavirus-Hit Market* (July 6, 2020), https://tinyurl.com/yc2s98mr. For investors, convertible bonds offer upside potential if the company's common stock appreciates and afford "a degree of indexation to rising consumer prices." The Economist, *Why Convertible Bonds Are the Asset Class for the Times* (July 10, 2021), https://tinyurl.com/2s45aedv. For these reasons, they are "well-suited to fast-changing conditions." *Id.* Since 2021, more than $270 billion in convertible bonds have been issued. *See ECM Highlights: FY22*, dealogic (Dec. 19, 2022), https://tinyurl.com/53vfdkjh.

Advisers, funds, and investors ultimately seek returns on investment rather than attempting to make a market. Investment opportunities may come from an SEC-registered broker or dealer who has been engaged by an issuer looking for investors. Opportunities also may come from a fund or adviser contacting a registered broker or dealer, seeking investments that meet particular criteria. Typically, investments are made through or with the assistance of a broker or dealer intermediary, not through a structure that positions the issuer as the customer. And typically the adviser, fund, or investor does not hold itself out as predominantly being in the business of matching buyers and sellers or of financing companies by issuing new securities.

B. Registered Investment Advisers And Funds Are Subject To Oversight By The SEC And Others.

Since 2010, investment advisers to private funds, or with assets under management that exceed $150 million, are required to register with the SEC—and are thus subject to SEC oversight and regulation. SEC, *Private Fund Adviser Overview* (Oct. 21, 2016), https://tinyurl.com/2s3udjsd. Advisers are examined for compliance by SEC staff and required to file re-

ports with the SEC, for example. SEC, *Investment Advisors Overview* (Mar. 31, 2017), https://tinyurl.com/y5dwcs7m (describing compliance and disclosure obligations); *see generally* Investment Advisers Act of 1940, 15 U.S.C. § 80b-1 *et seq.*

Private funds that hire registered investment advisers are also within the SEC's purview. Since 2011, the SEC has required registered investment advisers to disclose detailed information about the private funds they manage, including "fund size, use of borrowings and derivatives, strategy, and types of investors." SEC, Annual Staff Report Relating to the Use of Form PF Data (Dec. 9, 2022), https://tinyurl.com/2p8vpwzr. Private funds are also subject to securities laws when they raise money from investors. *See* 17 C.F.R. § 230.500 *et seq.* In addition, mutual funds and other entities are subject to the Investment Company Act of 1940, 15 U.S.C. § 80a-3, while pension funds may come under SEC scrutiny as well, *see* 17 C.F.R. § 245.101.

C. Registered Investment Advisers And Funds Are Different From Dealers And Are Regulated Differently.

Registered investment advisers and the private funds they manage are very different from dealers. They are subject to different regulatory frameworks, "have different types of relationships with investors, offer different services, and have different compensation models when providing investment recommendations or investment advisory services to customers." *Regulation Best Interest: The Broker-Dealer Standard of Conduct*, 84 Fed. Reg. 33,318, 33,319 (July 12, 2019).

Dealers typically hold themselves out as willing buyers and sellers of securities. They typically advertise and solicit buyers and sellers, or issuers, each of whom may be a dealer's customer or counterparty. Dealers also hold inventory (often acquired in bulk) to pair those who wish to buy and sell a particular security at different times. "A broker-dealer's recommendations may include recommending transactions where the broker-dealer is buying securities from or selling securities to retail customers on a principal basis or recommending proprietary products." *Id*; *see also XY*

Plan. Network, LLC v. SEC, 963 F.3d 244, 248 (2d Cir. 2020) ("[B]roker-dealers often provide advice and make recommendations about securities transactions and investment strategies."). "Investment advisers, on the other hand, typically provide ongoing, regular advice and services in the context of broad investment portfolio management." *Regulation Best Interest: The Broker-Dealer Standard of Conduct*, 84 Fed. Reg. at 33,319.

Dealers "effect securities transactions for customers, for which they typically charge a commission or other transaction-based fee," *XY Plan.*, 963 F.3d at 248 (citing 15 U.S.C. § 78c(a)(5)(A)), such as mark-ups/mark-downs. Advisers, on the other hand, receive compensation based on the advice they provide and the results they achieve. And private funds, which are "created to pool money from multiple investors … to make investments on behalf of the fund," have investors who are the fund's equity owners and benefit from its returns. SEC, Private Fund, https://tinyurl.com/2p8kxmmp (visited June 29, 2023). Funds, unlike dealers, do not have clients or customers: a fund is the adviser's client, a fund's investors do not transact on the opposite side of the fund, and a company in which the fund invests is not the fund's customer and is not in a customer relationship with the fund.

Registered investment advisers and funds are also regulated differently from dealers. Dealers are governed by the Exchange Act, not the Investment Advisers Act or the Investment Company Act. *See* 15 U.S.C. § 80a-1(b)(2) (distinguishing investment advisers from dealers); *id.* § 80a-3(a) (defining investment companies). Among other things, dealers must: maintain minimum net capital levels to satisfy customer claims (17 C.F.R. § 240.15c3-1); possess or control certain margin securities the broker-dealer carries for its customers' accounts (17 C.F.R. § 240.15c3-3); join a fund to insure customer accounts (*see* 15 U.S.C. § 78fff-4(c)); and implement safeguards to control risks associated with direct access to securities markets (17 C.F.R. § 240.15c3-5). These

rules are designed to protect broker-dealers' customers. But these rules have no utility as applied to funds, which have no customers, and may harm fund investors by imposing costs to comply with ill-fitting requirements without a corresponding benefit to investors, markets, or regulators.

II. This Court Should Hold, Consistent With The Text, History, And Structure Of The Exchange Act, That "Dealer" Means An Entity That Executes Customer Orders.

The SEC urges this Court to read the term "dealer" in the Exchange Act to reach anyone "engaged in the business" of "buying and selling securities." *See* SEC Opp. at 1, 7-9, 17. This expansive interpretation eschews bedrock principles of statutory construction in favor of a novel, hyper-literal, myopic reading that undermines the statutory text, historical context, and the SEC's own longstanding view of what constitutes "dealing." This Court should reject it.

A. The SEC's Interpretation Of "Dealer" Contravenes The Statutory Text, Its Own Guidance, And Well-Established Understandings.

The SEC's proposed interpretation of "dealer" flouts multiple rules of statutory interpretation and lacks a limiting principle. As Defendants explain, the SEC's reading of the statute contradicts the historical evidence about the meaning of the term "dealer" under the Exchange Act—which, along with the dealer registration requirements, was "crafted specifically to protect investing customers, and in-turn regulate firms who had customers." Dkt. 22 ("Morningview Br.") 6-7.

1. Dealers, Like Brokers, Effectuate Orders For Customers.

When Congress enacted the Exchange Act of 1934, there were only two methods of effectuating customer orders. A firm could trade "solely for the account of the customer," as an agent or "broker," or *with* the customer, on the opposite side of the transaction, as a dealer "act[ing] for [the dealer's] own account" as a principal "and not as agent for the customer." SEC, Report on the Feasibility and Advisability of the Complete Segregation of the Functions of Dealer and Broker, at XIV (1936), https://tinyurl.com/y6h3a4ts; *see also XY Plan.*, 963 F.3d at 248.

Prominent treatises at the time are full of own-account/others'-account references that distinguish the two ways of effectuating customer orders. *See, e.g.*, Charles F. Hodges, *Wall Street* 361 (1930) ("A dealer sells to and buys from a client whereas a broker buys and sells for the account of a client."); Charles Harrison Meyer, *The Law of Stockbrokers and Stock Exchanges and of Commodity Brokers and Commodity Exchanges* 32-33 (cumulative suppl. 1933) (noting that what "distinguishe[s]" the "dealer. . . from a broker" is that the dealer buys from or "sells to his customers … securities which he has purchased for his own account elsewhere").

The SEC itself used similar references in the same way. *See, e.g., G.L. Ohrstrom & Co.*, 1938 WL 33306, at *7 (SEC Dec. 16, 1938) (broker traded "for [the customer's] account," dealer traded "for [its] own account"); *E.H. Rollins & Sons, Inc.*, 1945 WL 73020, at *6 (SEC Feb. 22, 1945) (explaining "for the account of" was "characteristic of agency"). Early Commission rules reflected this distinction, requiring brokers and dealers to "disclose to [their] customer[s] . . . whether [they] [were] acting as a dealer for [their] own account," or "a broker" for the customer's account. Rules for the Regulation of Over-the-Counter Markets, 1936 WL 31460, at *6 (SEC Jan. 20, 1936). And the Commission acknowledged that although investment companies and investment advisers have a business model based on the purchase and sale of securities, they were not governed by rules that applied to "'brokers and dealers' only," 2 H.R. Doc. No. 76-279, at 1523 n.434 (1939), and "[f]ederal regulation" of investment advisers did "not exist," H.R. Doc. No. 76-477, at 31 (1939)—reflecting the understanding that broker-dealers execute customer orders.

Case law from the era confirms this understanding. *E.g., Donander Co. v. Comm'r*, 29 B.T.A. 312, 314-15 (1933) (dealer applies only "to a merchant who holds himself out to sell to customers"); *Harriman Nat'l Bank v. Comm'r*, 43 F.2d 950, 952 (2d Cir. 1930) (dealer "purchased securities to fill specific orders" and "h[eld] them for customers"). The common law meaning—

which Congress presumptively retained, *Universal Health Servs., Inc. v. United States*, 579 U.S. 176, 187 n.2 (2016)—distinguished between means of effectuating customer orders. *See Johnson v. Winslow*, 279 N.Y.S. 147, 156 (N.Y. Sup. Ct. 1935); *Weisbrod v. Lowitz*, 282 Ill. App. 252, 255 (1935); William O. Douglas et al., *Stock "Brokers" as Agents and Dealers*, 43 Yale L.J. 46, 60-61 (1933) (detailing factors distinguishing brokers and dealers, presupposing customer orders).

The interplay between "broker" and "dealer" in the securities laws confirms that both definitions referred to different means of effectuating customer orders. The terms "broker" and "dealer" are linked throughout the Exchange Act (*see, e.g.*, 48 Stat. at 882-897 §§ 3(a)(3), 7(c), 9(a)(3)-(5), 11(d)-(e), 12(a), 14(b), 17(a)-(b)), indicating that they have a related meaning, Antonin Scalia et al., *Reading Law: The Interpretation of Legal Texts* 198 (2012) (explaining canon that words are known by the company they keep). Indeed, the SEC does not distinguish between the two, requiring registration "as a broker-dealer," not as one or the other. 17 C.F.R. § 249.501(a); SEC Form BD, item 2.A, https://tinyurl.com/2p82stzb. The two definitions are also used specifically to impose customer protection requirements. For example, section 11(d) requires a broker or dealer to "disclose[] to [the] customer in writing… whether he is acting as a dealer for his own account" or "as a broker for [the] customer." 48 Stat. at 892, 15 U.S.C. § 78k(d).

Moreover, in 1999, Congress revised the definition of "dealer" by amending the bank exemption from the definition in the Exchange Act and simultaneously amending the definitions in the Investment Company Act and the Investment Advisers Act to track the new Exchange Act definition. *Id.*; Pub. L. No. 106–102, §§ 202, 216, 219, 113 Stat 1338 (Nov. 12, 1999). Critically, this revision left the substantive language of the Exchange Act unchanged, aside from the change to the bank exemption—leaving undisturbed settled precedent that only businesses buying and selling securities to execute customer orders are dealers, and not adopting a position like the SEC

now advances. *Aetna Life Ins. Co. v. Big Y Foods, Inc.*, 52 F.4th 66, 75 (2d Cir. 2022) ("Congress is presumed to be aware of an administrative or judicial interpretation of a statute and to adopt that interpretation when it re-enacts a statute without change." (citing Supreme Court precedent)).

The SEC's blinkered approach here fails to recognize the *customer*-focused meaning of "broker" and "dealer." Contrary to the original limited meaning, the SEC's new near-limitless reading would make a dealer out of many advisers, funds, and other market participants—subjecting them to rules that are inapplicable to their businesses because they lack customers. *See supra* I.C. Because that result cannot be squared with the historical context in which Congress enacted the Exchange Act in 1934, it is not a permissible way to interpret the meaning of "dealer" under the Exchange Act today. *See Sackett v. EPA*, 143 S.Ct. 1322, 1338 (2023) ("The meaning of a word 'may only become evident when placed in context.'").

2. The Statutory Exemption Provides That Traders And Entities That Do Not Have Customers Are Not "Dealers."

The Exchange Act's exemption for activity "not as a part of a regular business," 15 U.S.C. § 78c(a)(5)(B), also makes clear that traders and investors (who do not have customers) cannot be characterized as dealers. Elsewhere, the SEC has conceded that the exception applies regardless of how frequently a trader trades if they accept risk. *See* SEC Sur-Reply 4-6, *Almagarby*, No. 21-13755 (11th Cir. Dec. 12, 2022), ECF 51-2; *Further Definition of "As a Part of a Regular Business" in the Definition of Dealer and Government Securities Dealer*, SEC Release No. 34-94524, 87 Fed. Reg. 23,054, 23,058-59, 23,059 nn.53-56 (proposed Apr. 18, 2022) ("*Proposed Rule*"). Read in context, the "regular business" exemption further shows that a "dealer" only includes those that trade for their own account to fill *customer* orders.

When the Exchange Act was adopted in 1934, "many" tax-related court rulings interpreted the phrase "not in the course of an established business," which appeared in the regulatory definition of "dealers in securities," to mean that traders who did not have an established place of business to serve customers could not be dealers—regardless of the frequency of their trading and whether the trading was for a partnership or other business organization. *Schafer v. Helvering*, 299 U.S. 171, 173-74 & n.1 (1936) ("The meaning of 'dealer in securities'. … is limited to one who, as a merchant, buys and sells securities to customers."); *see Sec. Allied Corp. v. Comm'r*, 95 F.2d 384, 386 (2d Cir. 1938) (company not a dealer when "[i]t had no place of business to which customers could come to buy"); *Wilson v. Comm'r*, 76 F.2d 476, 478 (10th Cir. 1935). Congress had these settled interpretations in mind when it paraphrased that language in the "regular business" exemption in the Exchange Act. *See* Scalia et al., *supra* (describing "Prior-Construction Canon").

That historical context is critical to understanding the Exchange Act's meaning. To a contemporary reader familiar with democratized, professionalized investing, a business that buys and sells stock to earn trading profits may seem like a "regular business." But in 1934, in the wake of the market crash of 1929, traders who bought and sold securities were seen as speculators—distinct from professional broker-dealers who achieved profits through commissions, fees, or the spread when executing customer orders. The exemption thus makes clear that these entities that engaged in investment or speculation are not "dealers" under the Exchange Act. Failing to account for that exemption as it was historically understood is further reason to reject the SEC's interpretation. *See MCI Telecomms. Corp. v. Am. Tel. & Tel. Co.*, 512 U.S. 218, 228 (1994) ("the most relevant time for determining a statutory term's meaning" is when it became law).

3. The SEC Ignores Differences Between The Securities Act And The Exchange Act And Relies On Inapposite, Out-of-Circuit Case Law.

The SEC relies heavily on the Eleventh Circuit's decision in *SEC v. Big Apple Consulting USA, Inc.*, 783 F.3d 786 (11th Cir. 2015). *See* SEC Opp. at 9-10, 14-15, 17-18. But no court in the Second Circuit has adopted its analysis and, as Defendants explain, *Big Apple* is not controlling because it interpreted "dealer" under Securities Act § 5, not Exchange Act § 15—the operative provision here. *See* Dkt. 25 ("Morningview Reply") 5-6. That distinction makes a difference.

The Securities Act, enacted in 1933, has no exemption that limits the definition of "dealer"—it explicitly includes "trading" and lumps together both brokers and dealers in a single, catch-all definition. *See id.* at 5 (citing 15 U.S.C. § 77b(a)(12)). By contrast, just one year later in 1934, Congress crafted a more nuanced definition in the Exchange Act—defining "broker" and "dealer" separately, using language that in context referred to customers, eliminating any reference to "trading," in the definition of "dealer," and adding the exemption that makes clear that investors, speculators, and other traders who are transacting "not as a part of a regular business" are not "dealers." 15 U.S.C. § 78c(a)(5)(B). Disregarding those textual differences and equating the definition of "dealer" under the Securities Act with the definition in the Exchange Act ignores that "[w]here the words of a later statute differ from those of a previous one on the same or related subject, the Congress must have intended them to have a different meaning." *Burrus v. Vegliante*, 336 F.3d 82, 89 (2d Cir. 2003); *see Wis. Cent. Ltd. v. United States*, 138 S.Ct. 2067, 2071 (2018) (noting "differences in language" between companion statutes "convey differences in meaning").

There are also important structural reasons why the definition of "dealer" in the Exchange Act is narrower than the corresponding definition in the Securities Act. The Securities Act definition applicable in *Big Apple* is relevant where, as there, a defendant is engaged in an *unregistered* distribution of *unregistered* shares (for example, penny stocks that are less regulated and more

susceptible to fraud). By contrast, the Exchange Act's "dealer" definition is not so limited, and also applies to *registered* distributions (for example, blue-chip stocks that are more heavily scrutinized). It is logical that Congress would more tightly regulate the former than the latter.[2]

If the term "dealer" were construed as broadly as the SEC suggests, it could wrongly categorize *thousands* of mutual funds, private funds, insurance companies and others as "dealers"—subjecting them and their investors to costly capital requirements and customer protection rules that make no sense for entities that lack customers. Even day traders or retirees would potentially face dealer liability. "Without legal limitations, market participants [would be] forced to rely on the reasonableness of the SEC's litigation strategy, but that can be hazardous." *Dirks v. SEC*, 463 U.S. 646, 664 n.24 (1983). Indeed, the Supreme Court—in unanimous or near-unanimous opinions—has repeatedly recognized the importance of scrutinizing SEC actions.[3] Administrative agencies like the SEC cannot "assert[] highly consequential power beyond what Congress could reasonably be understood to have granted" based on "a merely plausible textual basis"—especially when the agency's "newly uncovered" regulatory authority has "conveniently enabled it" to pursue a theory that was previously unsupported. *W. Va. v. EPA*, 142 S.Ct. 2587, 2609, 2614 (2022).

[2] Although *Big Apple* noted in a footnote that the "dealer" definition in the Securities Act and the Exchange Act are "similar," that was *dicta* that this Court should not rely on in the face of meaningful differences discussed above. Plus, the defendant there had "abandoned" a challenge to its "dealer" status under the Exchange Act and the parties did not brief the issue. 783 F.3d at 806, 809 n.11.

[3] *See Axon Enter., Inc. v. FTC*, 143 S.Ct. 890, 900 (2023) (unanimously affirming *Cochran v. SEC*, 20 F.4th 194 (5th Cir. 2021), allowing court challenges to SEC in-house proceedings before they concluded); *see also Lucia v. SEC*, 138 S.Ct. 2044, 2053-54 (2018) (reversing D.C. Circuit, 7-2, invalidating SEC in-house adjudications); *Liu v. SEC*, 140 S.Ct. 1936, 1946 (2020) (vacating Ninth Circuit, 8-1, limiting SEC's disgorgement power); *Kokesh v. SEC*, 581 U.S. 455, 465-67 (2017) (unanimously reversing Tenth Circuit, rejecting SEC's view that statute of limitations did not apply to disgorgement); *accord Gabelli v. SEC*, 568 U.S. 442, 454 (2013) (unanimously reversing Second Circuit, rejecting discovery rule in SEC actions).

That is what the SEC proposes to do here. Nearly ninety years after the Exchange Act's passage—and after years of not requiring investment advisers, funds, and other investment vehicles to register as dealers—the SEC now sees "dealer" in a new light. Its long-running failure to advance the position it now asserts is strong proof that the position lacks merit. *Cf. id.* at 2610-14; *see also SEC v. Federated Alliance Grp., Inc.*, 1996 WL 484036, at *5 (W.D.N.Y. Aug. 21, 1996) (rejecting SEC's "excessively broad definition of a dealer" that "would embrace as a dealer every securities trader who makes money through buying and selling of securities."); *Goldstein*, 451 F.3d at 878-83 (rejecting SEC's attempt to redefine the term "client" in the Investment Advisers Act when the SEC could not "justify departing from its own prior interpretation" and sought to impose new registration requirements as a "hook [for] more comprehensive regulation of hedge funds").

For these reasons, this Court should hold that "dealer" status under the Exchange Act requires evidence of executing customer orders—not merely purchasing and selling securities. The complaint here fails to allege that Defendants were in the business of buying or selling to execute customer orders. While the SEC alleges that Defendants purchased convertible securities from penny-stock issuers (Opp. at 21), that does not make the issuers Defendants' "customers." Traders frequently purchase newly issued securities (including convertible securities) from issuers amidst a broader trading strategy—which makes that activity fit squarely within the "regular business" exemption and insufficient to trigger "dealer" status. Indeed, the SEC does not appear to dispute that many of Defendants' transactions were not made on behalf of issuers, but instead represented Defendants' own trading activity. The SEC thus fails to allege Defendants were in the "regular business" of executing *customer* orders—which is necessary to establish "dealer" liability.

B. Revising The Established Meaning Of "Dealer" Is Up To Congress, Or The SEC—If It Can Act In Compliance With Applicable Requirements.

Convertible transactions are not new. For years, with the SEC's blessing, companies have issued convertible debt to investors, who converted the debt into stock at a discount and resold it at an advantageous time. If the SEC now wishes to root out specific practices by specific types of market participants, it has multiple ways to attempt to do so. Bringing ad hoc enforcement actions based on a newly devised interpretation of what it means to be a "dealer" is not one of them.

Congress, of course, is uniquely situated to alter the definition of "dealer" or expand the SEC's related regulatory reach. *See W. Va.*, 142 S.Ct. at 2609, 2613. Indeed, as the Supreme Court recently noted, "Congress remains free to revise the securities laws at any time" to address "any … development." *Slack Techs., LLC v. Pirani*, 143 S.Ct. 1433, 1442 (2023).

If the SEC now takes issue with companies holding themselves out as a source of capital to issuers and then selling the newly issued securities they receive back into the market (*see* SEC Opp. at 2, 8, 22-23), then it could choose to revise Rule 144, which created a safe harbor against underwriter liability if securities are held for six months. 17 C.F.R. § 230.144(d)(1)(i); *see Revisions to Rules 144 and 145*, 72 Fed. Reg. 71,546, 71,561-62 (Dec. 17, 2007) (adopting 6-month safe harbor after concluding that the prior 12-month safe harbor made it too difficult for small issuers to raise capital). If the SEC believes fraud is underfoot, or that an issuer's choice to finance itself using convertible bonds is problematic, it can wield existing antifraud authority.

The SEC seems to have instead chosen to pursue through rulemaking a new vision of what it means to be a "dealer." *See Proposed Rule*, *supra*. Such an effort could be appropriate if the SEC were filling genuine gaps in a statutory scheme or clarifying ambiguities, within the scope of the authority delegated by Congress and in compliance with applicable rules—such as properly balancing costs and benefits and accounting for stakeholder perspectives. *See W. Va*, 142 S.Ct. at

2608-09; 5 U.S.C. § 706(2)(A); 15 U.S.C. §§ 78c(f) (requiring the SEC to consider "whether the action will promote efficiency, competition, and capital formation"), 78w(a)(2) (mandating the SEC to consider "the impact any such rule or regulation would have on competition").

There are many good reasons to think the SEC's regulatory efforts regarding the "dealer" definition fail those requirements. For example, the analysis above, the unprecedented authority the SEC asserts after nearly ninety years, and the "economic and political significance of that assertion," strongly suggest the SEC lacks authority to interpret "dealer" to cover wide swaths of the financial industry. *See W. Va.*, 142 S.Ct. at 2608-09. Plus, the record before the SEC reflects that the proposed rule will impose many costs but yield few (if any) benefits. *See, e.g.*, AIMA Comment Letter, File No. S7-12-22 (May 27, 2022), https://tinyurl.com/5n7486j5; *see also* Craig Lewis, *The SEC's Proposed Rules for Further Definition of "As a Part of a Regular Business" in the Definition of Dealer and Government Securities Dealer* (Dec. 2022), https://tinyurl.com/38w2s4hj (former SEC Chief Economist and Director of the Division of Economic and Risk Analysis highlighting flaws in proposed rule and harm it may cause to markets and investors). That casts a cloud over the SEC's questionable choice to sidestep Congress while simultaneously pursuing enforcement actions advancing an expansive and novel interpretation of what it means to be a "dealer."

Whether a revised definition is effectuated through legislation or a proper rulemaking, the result will likely be better than ad hoc enforcement actions. On the front end, decisionmakers "can conduct factual investigations, can consult with affected parties, [and] can consider how their experts have handled similar issues over the long course of administering a regulatory program." *Kisor v. Wilkie*, 139 S.Ct. 2400, 2413 (2019); *see Long Island Care at Home, Ltd. v. Coke*, 551 U.S. 158, 167-68 (2007). On the back end, the result should (in theory) provide clarity about what the rule is and how to follow it. And if the resulting rule is defective, judicial review is available

and the decisionmakers can be held politically accountable. *See Kisor*, 139 S.Ct. at 2413; *Pauley v. BethEnergy Mines, Inc.*, 501 U.S. 680, 696-97 (1991).

On the other hand, cherry-picked enforcement actions create a risk that markets and market participants will be whipsawed by the SEC's arbitrary discretion, subject to a patchwork of inconsistent interpretations of the law, and beset with uncertainty and unpredictability. Indeed, Congress has expressed a preference that interpretive issues related to complex regulatory schemes not be resolved "piecemeal by litigation." *Kisor*, 139 S.Ct. at 2413-14. That provides further reason for this Court to reverse and to reject the SEC's attempt to resolve perceived issues around the meaning of "dealer" through this action.

Regardless of the vehicle, the SEC may not misconstrue the text, history, and settled understanding of the Exchange Act. Nor may the SEC exceed its authority to target activity it may dislike and transform all businesses that buy and sell securities into lawbreakers. The law does not allow the SEC to force a square peg into a round hole in the name of investor protection (SEC Opp. at 4-5) by redefining "dealer" to capture activity that does not satisfy the statutory definition.

III. The Court Should At Minimum Ground Any Decision In The SEC's Factors That Distinguish "Dealers" From Registered Investment Advisers And Funds.

As explained above, this Court has many strong grounds to reject as a matter of law the SEC's broad view of what it means to be a "dealer" under the Exchange Act. *See supra* at Part II; *see also* Morningview Br. 10-13 (demonstrating how the SEC's newfound interpretation of "dealer" contradicts the SEC's own statements and actions over the years). Morningview also argues the SEC's factual allegations are not enough to state a claim. Morningview Reply 8-10.

If this Court finds the SEC Complaint states a claim, it should ground that decision in the factors that the SEC concedes "Courts and the SEC have, over time, applied … to distinguish dealers from traders." SEC Opp. at 19. The Court should not endorse any argument that the SEC

can impose "dealer" liability on literally "anyone who has operated a company at a regular place of business that offers services to the public for a profit." *Id.* Rather the Court should follow the New York courts that have held that "[w]hether an individual falls within [the Exchange Act's dealer] definition similarly requires analysis of a variety of factors." *Dervan v. Gordian Grp. LLC*, 2017 WL 819494, at *10 (S.D.N.Y. Feb. 28, 2017).[4]

Doing so, and declining to endorse the SEC's overly broad reasoning that satisfying even one factor may be enough to qualify as a dealer (SEC Opp. at 19-20), would help avoid sweeping and serious consequences for markets and market participants whose activities differ from what the SEC alleges it believes makes Morningview a "dealer." For example:

1. Registered investment advisers and funds typically do not advertise, have customers, or repeatedly "cold" contact issuers or customers in bulk while "[holding] themselves out to the public" as being in the business of buying and selling securities to or from their customers. SEC Opp. at 2, 8, 21-23; see also *EMA Fin.*, 2022 WL 4237144, at *5. While they may attend conferences and publicly express a general interest in investments, as would be unsurprising for investment firms, alleging those vanilla facts alone cannot be enough to trigger the weighty burdens that come with dealer status.

2. Although buying and selling convertible notes is a component of many registered investment advisers' and funds' operations, their "entire" business model is not focused on "convert[ing] … debts into newly issued shares of stock" or "turn[ing] a profit by selling newly issued shares into the market." SEC Opp. at 17, 21-22. Nor do they aim to provide liquidity to the market by pairing buyers and sellers.

3. Registered investment advisers and funds do not typically focus on buying "debt securities directly from issuers (acting as principal)" they have solicited as customers, as opposed to investing through intermediaries. *Id.* at 22; *see also Hansen*, 1984 WL 2413, at *10 (providing that a "relevant" factor is "selling" "securities of other issuers"). Investment advisers' clients are the funds they advise, and the funds have investors but do not have clients or customers at all. *See supra* at I.C.

[4] *See also EMA Fin., LLC v. AppTech Corp.*, 2022 WL 4237144, at *5 (S.D.N.Y. Sept. 13, 2022); *Federated Alliance Grp.*, 1996 WL 484036, at *4-5. *Accord Rhee v. SHVMS, LLC*, 2023 WL 3319532, at *8 (S.D.N.Y. May 8, 2023) (applying factors articulated in *SEC v. Hansen*, 1984 WL 2413 (S.D.N.Y. Apr. 6, 1984)).

4. Registered investment advisers and funds do not serve as intermediaries between issuers and investors or service customers. *See* SEC Opp. at 2, 22-23; *see also Hansen*, 1984 WL 2413, at *10. They most often trade through registered broker-dealer intermediaries for investment purposes. *See supra* at I.C.

5. Registered investment advisers and funds are already subject to SEC oversight and advisers are required to, among other things, disclose detailed information about funds they manage. *See supra* at I.B.[5]

Any decision in this case should be grounded in its specific allegations—not categorically label *any* business buying and selling securities as a "dealer." Adopting these limitations will avoid an overly broad holding and the chaos that could flow from upending settled expectations of those who have relied on precedent and SEC guidance construing the term "dealer."[6]

CONCLUSION

For the foregoing reasons, amici urge this Court to grant Defendants' motion to dismiss and issue a narrow opinion that avoids causing harm to markets and market participants.

Date: July 6, 2023

Respectfully submitted,

Anthony S. Barkow (N.Y. Bar #4745220)
Charles D. Riely (N.Y. Bar #4091609)
Jenner & Block LLP
1155 Avenue of the Americas

/s/ Gabriel K. Gillett
Gabriel K. Gillett (N.Y. Bar #5011705)
Counsel of Record
Jenner & Block LLP

[5] Certain facts the SEC has highlighted do not provide a meaningful basis for determining dealer status. *See, e.g.*, SEC Opp. at 8. Whether pricing is fixed or variable does not matter; convertible securities use both. Whether shares are issued at a discount does not matter; some investments like secondary offerings are always at a discount. Whether securities are sold at the earliest opportunity does not matter; "flipping, alone, is not prohibited under the federal securities laws." SEC, Investor Bulletin: Investing in an IPO 5, https://tinyurl.com/y6neb23x (visited June 29, 2023).

[6] Defendants' motion does not separately seek dismissal of the SEC's request for disgorgement. Even if the Court does not dismiss the SEC's claims, amici note that disgorgement will not be an available remedy here because the SEC does not allege that Defendants' failure to register as a dealer caused them to earn any profits, attract any investors, harm any investors, or impair any investments. *See Liu*, 140 S.Ct. at 1941-42, 1947-49 (tying disgorgement to "ill-gotten gains" and harm to victims); *SEC v. Hallam*, 42 F.4th 316, 329 & n.32 (5th Cir. 2022) (explaining that disgorgement aims to reclaim "a reasonable approximation of profits causally connected to the violation."); *Alvarez v. United States*, 862 F.3d 1297, 1302 (11th Cir. 2017) (noting registration failure "had no effect" on investors).

New York, NY 10036
(212) 891-1662
abarkow@jenner.com
criely@jenner.com

353 North Clark Street
Chicago, IL 60654
(312) 840-7220
ggillett@jenner.com

Counsel for Proposed Amici Curiae Alternative Investment Management Association, Ltd., Trading and Markets Project, Inc., and the National Association of Private Fund Managers

CERTIFICATE OF COMPLIANCE

This brief complies with the requirements of Local Civil Rule 11.1(a) and (b).

Date: July 6, 2023

/s/Gabriel K. Gillett
Gabriel K. Gillett

CERTIFICATE OF SERVICE

I, Gabriel K. Gillett, an attorney, hereby certify that on July 6, 2023, I caused the attached **Brief of Alternative Investment Management Association, Ltd., Trading and Markets Project, Inc., and the National Association of Private Fund Managers as Amici Curiae in Support of Defendants and Dismissal** to be electronically filed with the clerk of the Court for the United States District Court, Southern District of New York using the CM/ECF system. I certify that all participants are registered CM/ECF users and that service will be accomplished by the CM/ECF system.

/s/Gabriel K. Gillett
Gabriel K. Gillett