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UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF CALIFORNIA

RICHARD EDELMAN,

Plaintiff,

v.

UNITED STATES SECURITIES AND EXCHANGE COMMISSION,

Defendant.

Case No.: 15-CV-2750-BEN-BGS

PLAINTIFF'S REPLY BRIEF IN SUPPORT OF MOTION FOR PARTIAL SUMMARY JUDGMENT

Date: March 13, 2017
Time: 10:30 a.m.
Ctrm: 5A
Judge: Hon. Roger T. Benitez

I. Introduction

The SEC does not make a single valid point in opposing Edelman's motion for summary judgment. To begin with, its proof that it conducted an adequate search is vague, conclusory, ambiguous, and hearsay. Its affiant is an SEC attorney who claims no personal knowledge of the records to be searched or the search itself. The SEC cites no authority upholding such a search and we can find none. And then there is a nagging question: how could the SEC generate only a handful of records in an investigation of fraud claims by hundreds of elderly investors involving tens of thousands of records generated over 18 months?

The SEC now clings to any record that gives a clue why it allowed Malkin Holdings and its billionaire owner to divest investors of their interests in the Empire State Building, an investment they made five decades ago or inherited from their parents. Instead of evidence, the SEC offers mystery in clinging to the most probative record why it closed the MUI investigation: the Case Closing Recommendation ("CCR") of the SEC Enforcement attorneys who handled the investigation. The SEC claims the CCR is merely deliberations that never resulted in a writing closing the MUI. That presents another mystery: what happened to the MUI if it was never closed? Is the SEC still deliberating four years after the IPO closed?

And then there are the records the SEC obtained from Malkin Holdings. The SEC has reversed its grounds for withholding these records. It told this Court in its opening brief that the District Courts in the Ninth Circuit have applied *National Parks & Conservation Asso. v. Morton*, 498 F.2d 765 (D.C. Cir. 1974) in deciding whether an agency could withhold records under Exemption 4, but no Ninth Circuit District Court ever followed *Critical Mass Energy Project v. Nuclear Regulatory Comm'n*, 975 F.2d 871 (D.C. Cir. 1992). D. 22-1 at 8. After Edelman's brief demonstrated Ninth Circuit cases applying *National Parks* refute the SEC's assertion of Exemption 4, the SEC flip-flopped: it now invites this Court to be the *first* District Court in the Ninth Circuit to apply *Critical Mass*. We submit this is an invitation the Court should decline.

The SEC contends its track record of hostility to FOIA is irrelevant. According to the SEC, it is irrelevant that it destroyed records of ten thousand MUIs in violation of the Federal Records Act, that Congress—without a dissenting vote—repealed the SEC-sponsored statute allowing it to withhold investigative files, that the U.S. Senator who chairs the Senate Committee with oversight of all agencies' compliance with FOIA singles out the SEC's hostility towards FOIA, that the Commission empowered by Congress to investigate the causes of the 2008 financial crisis found the SEC's failures were a significant contributing cause to the crisis. Edelman disagrees. These factors all point to the public policy underlying FOIA: transparency. In overruling the SEC's claimed exemptions to the records sought in *Aguirre v. SEC*, 551 F. Supp. 2d 33, 56 (D.D.C. 2008), the District Court quoted the Senate Report on transparency:

> Maintaining transparency, public confidence in the integrity of our securities market, and a level playing field for the average investor are important goals of the SEC's enforcement practices.…Because those events may be forgotten by a new generation working on Wall Street, it is important for Congress to continue to ensure that regulators have an appropriate focus on preventing a recurrence of such activity and to effectively utilize the authority and tools given to them under statutes and in the funding process.

Justice Louis D. Brandeis said it best: “Sunlight is said to be the best of disinfectants; electric light the most efficient policeman."

II. The SEC Failed to Conduct a Search Reasonably Calculated to Uncover All Records Responsive to Edelman's Requests

To meet its burden, the SEC must "demonstrate that it has conducted a 'search reasonably calculated to uncover all relevant documents.'" *Zemansky v. U.S. Envtl. Prot. Agency,* 767 F.2d 569, 571 (9th Cir. 1985). See also *Yonemoto v. Dep't of Veterans Affairs,* 648 F.3d 1049, 1057 (9th Cir. 2011); 5 U.S.C. § 552(a)(3)(C)-(D). The SEC failed to establish each and every link in this evidentiary chain.

The SEC argues that the two declarations by Carin Cozza ("Cozza"), an attorney in the SEC's Office of the General Counsel ("OGC"), satisfy its burden. Fed. R. Civ. P. 56(c)(4) ("Rule 56") defines the form of the proof in summary judgment motions. It

states that "an affidavit or declaration used to support or oppose a motion [for summary judgment] must be made on personal knowledge, set out facts that would be admissible in evidence, and show that the affiant or declarant is competent to testify on the matters stated." Edelman agrees with the SEC that *Lahr v. NTSB*, 569 F.3d 964, 990 (9th Cir. 2009) allows an agency to rely on "an affidavit from an agency employee responsible for supervising a FOIA search" to satisfy Rule 56's personal knowledge requirement. However, Rule 56 requires the affiant to state "facts that would be admissible evidence" and be "competent to testify on the matters stated." In the context of a FOIA case, the affidavits must be detailed, nonconclusory, and not impugned by evidence of bad faith. *Citizens Comm'n on Human Rights v. FDA*, 45 F.3d 1325, 1328 (9th Cir. 1995).

The Cozza declarations fail to meet these standards in multiple ways. First, neither Cozza declaration establishes she is competent to testify that the search was reasonably calculated to uncover all relevant documents. To begin with, no one can conduct such a search unless he or she knows what records are kept, who keeps them, where they are kept, in what format they are kept, and how they are organized. Cozza's declaration offers only a conclusion: "I am also familiar with the Commission's procedures for responding to and searching for documents responsive to FOIA requests." D.22-2 ¶ 1. The SEC is a large agency with multiple divisions and offices located in multiple metropolitan areas around the country. Cozza's declaration fails to establish she knows how the different divisions and offices keep their records. Hence, her declaration fails to prove with "detailed, nonconclusory" statements, as required by *Citizens*, 45 F.3d at 1328, that she knows how such a search should be conducted.

Cozza's declarations also fail to satisfy the "personal knowledge" standard of *Lahr,* 569 F.3d at 990, which requires "an affidavit from an agency employee responsible for supervising a FOIA search." Cozza neither conducted nor supervised such a search. Her first declaration states "FOIA Lead Research Specialist Jason Luetkenhaus verified that the Commission had an investigation titled *In the Matter of Empire State Realty Trust*, MNY-08894." D.22-2, ¶ 3. Edelman objected to this statement in his opening brief on

dual grounds: it was not a description of a search and Cozza lacked personal knowledge of the subject. D. 23-1 at 12 and 11.

Cozza's second declaration proves she did *not* conduct a search. It reads:

> FOIA Lead Research Specialist Jason Luetkenhaus searched the Commission's internal databases and contacted staff in the Commission's New York Regional Office ("NYRO"). Based on his research, he determined that the specified investigation, MNY-0889, was the only SEC investigation concerning Empire State Realty Trust.

D. 25-1, ¶ 3. Other SEC records confirm FOIA Specialist Luetkenhaus conducted the search, not Cozza. Cozza is a staff attorney in the SEC's Office of the General Counsel ("OGC"). D. 22-2, ¶ 1. She reviews administrative appeals from the SEC's FOIA Office. *Id.* The FOIA Office completed its review of Edelman's appeal on September 28, 2015. D. 1-10, Ex. 9 to complaint. Edelman appealed on October 23, 2015. D. 1, ¶ 18. Thus, Cozza first became involved in the case months after the FOIA Office conducted its search. Further, Luetkenhaus and Cozza have different reporting chains all the way to the SEC Chairman. Aguirre Supplemental Declaration ("Aguirre Dec."), ¶¶ 3-5.

The SEC cites no case from any circuit where a court held that vague, ambiguous, conclusory, and hearsay declarations, such as those submitted by the SEC, entitled an agency to a summary judgment that it had conducted an adequate search. In *Our Children's Earth Found. v. Nat'l Marine Fisheries Serv.,* 2015 U.S. Dist. LEXIS 94997 (N.D. Cal. July 20, 2015), the District Court rejected a declaration similar to Cozza's, because it was "simply relaying hearsay regarding the search" conducted by someone else. The SEC's reliance on C*ouncil on American-Islamic Relations v. FBI*, 749 F. Supp. 2d 1104, 1119 (S.D. Cal. 2010) is misplaced, because the affiant conducted the search, his affidavit was detailed and nonconclusory, and the hearsay was limited to the confirmation an investigation existed for the purpose of Exemption 7(a).

Moving beyond the SEC's failure to establish Cozza had personal knowledge of the search, it also has failed to establish the search was reasonably calculated to locate all responsive records. Preliminarily, Edelman notes the volume of records generated by the

SEC is tiny in comparison with the potential issues Enforcement had to investigate. The SEC has identified only 27 records generated by Enforcement during the MUI.[1] Of these, 26 are handwritten notes or contain handwritten notes.[2] Did no one generate a factual or legal memorandum? Where are the emails? The issues under investigation were complex and the potential harm major: an internal SEC memorandum establishes that hundreds of investors complained about the IPO (Edelman Suppl. Dec., ¶ 3, Ex. 32); a class action based on the underlying facts settled for $55 million (D.23-1 at 6), implying the harm was significant; almost 3,000 elderly retail investors were potential victims; the SEC received at least 64,000 pages of records; the consolidation of ESBA extended over 18 months and involved hundreds of filings. And this generated only handwritten notes.

Cozza's vague, conclusory, and hearsay statements may cover over responsive records in countless ways. It is unknown (1) how Luetkenhaus determined there was only one investigation; (2) what records he requested; (3) whether he spoke with anyone who worked on the investigation (4) whether he spoke with staff who store records; and (5) why he reduced his estimate of responsive pages from 9,000 to 1,442.

There are two other glaring gaps in the SEC's search. First, there is no evidence anyone contacted the SEC's Office of Information Technology ("OIT") to search responsive electronic records, including emails, as the express language of FOIA requires. 5 U.S.C. § 552(a)(3)(C). Likewise, the SEC offers no competent evidence that it searched for other investigations concerning ESRT. Item 48 of the Vaughn identifies Enforcement notes of a "to do list for multiple investigations." Aguirre Dec., ¶ 7.A.

Cozza's declaration does not merely fail to comply with *Zemansky* and *Citizens*, the express language of FOIA, and the SEC's regulations relating to FOIA. It also fails to follow the SEC's own practices. The most recently published decision in Lexis involving an SEC search is Edelman's earlier FOIA case, *Edelman v. SEC*, 172 F. Supp. 3d 133

[1] The Vaughn index identifies 26 records generated by the SEC (Doc. Nos. 24, 25 and 27-50) and one more was produced, the Feb. 20, 2013, letter.

[2] Doc. Nos. 24, 27, 29-31, 33-38 and 40-49 are handwritten notes; Doc. Nos. 28, 32, 39 and 50 contain handwritten notes.

(D.D.C. 2016). The SEC's declarations in that case sharply contrast with Cozza's declarations in this case. The SEC did it by the book in the D.C. case. The affiant actually conducted the search: he contacted liaisons in the SEC's different divisions who contacted staff involved in the case, and requested OIT to search relevant email accounts and databases with search terms. Edelman Suppl. Dec., ¶¶4-7, Ex. 33-36. The affiants in the case the SEC primarily relies upon, *Lahr*, did the same. *See* Plaintiff's Request for Judicial Notice, Dkt. No. 26, ¶ 1, Exs. 1-3

III. The SEC Should Release Its Records of the ESRT MUI or Investigation

The SEC has enwrapped its MUI of ESRT in a mystery: what happened to it? According to Item 52 of the Vaughn Index, Enforcement staff generated a CCR on May 3, 2013, and took no further action. Solving the mystery is highly relevant, because the SEC claims it need not release the CCR under *NLRB v. Sears, Roebuck, & Co.*, 421 U.S. 132 (1975) on the ground the CCR did not result in a case closure. D. 25, at 4. Both the Vaughn Index and the SEC's brief leave the issue dangling. The case must have been closed: the SEC would assert Exemption 7(A), which is nearly bullet proof, and released nothing if the MUI was still open.

Only the FOIA Office offers a clue with its April 1, 2015, letter to Edelman:

> We have been advised that the Case Closing Recommendation is the Case Closing Report for matters under inquiry (MUIs). Effective in February 2013, a separate Case Closing Report is not required to close a MUI, and in this matter a Case Closing Report was not produced.

D. 1-17 at 2. Who advised the FOIA Office that a CCR would be not be required after February 2013?

This letter only heightens the mystery. Edelman can find no record that the SEC changed its record keeping of MUIs in February 2013. How the SEC maintained its MUI records was a highly sensitive issue for the SEC in 2013. For 17 years, the SEC destroyed its records of MUIs. That process stopped in 2011 when the SEC attorney tasked with destroying them, represented by Plaintiff's counsel, raised his concerns that the SEC was violating the Federal Records Act with the SEC's Inspector General, and the National

Archives and Records Administration ("NARA"). NARA, the SEC IG, and Congress rebuked the SEC for destroying federal records.[3] In this context, it is suspicious that the SEC modified its procedures for keeping records and closing MUIs with no paper trail.

The SEC procedure for handling MUIs is discussed in the SEC Enforcement Manual: "To close the MUI, the assigned staff should enter a closing narrative in Hub explaining why the matter is being closed and request that their Case Management Specialist designate the MUI closed in hub."[4] In another FOIA case where Edelman's counsel represented an SEC attorney, the issue arose how the SEC's New York Regional Office closed MUIs. An experienced attorney in the SEC's OGC informed Edelman's counsel in November 2013: "Until the last few years, there was no form to close a MUI. Before the HUB was introduced, the MUI was closed in CATs without text. *Now, closings are entered into HUB, and we have a record of that* (emphasis added)." Aguirre Dec., ¶ 6, Ex. 37. Consequently, HUB incorporates the recommendations of senior staff why an investigation is closed. Hence, assuming the MUI was closed, the SEC should release the HUB statement and the CCR.

But there is another possibility. The SEC assumes—without stating it as fact—that the MUI was not converted to an investigation. The SEC Enforcement Manual directs that MUIs open for more than 60 days should be converted to investigations. *Id.*, ¶ 7.B. The SEC Vaughn Index shows SEC *Enforcement* attorneys worked on an ESRT investigation from March 2012 through at least May 2013, a period of 14 months. Further, the SEC letter of February 20, 2013, confirms a MUI was open at that time and the Vaughn index confirms it was still open on May 22, 2013, a period of 92 days. Both periods exceed the 60 days within which Enforcement should convert a MUI into an investigation.

[3] See: https://www.archives.gov/press/press-releases/2011/nr11-170.html; https://www.sec.gov/foia/docs/oig-567.pdf and http://www.grassley.senate.gov/news/news-releases/sec-freezes-document-destruction-after-grassley-whistleblower-inquiry.

[4] Enforcement Manual, Nov. 1, 2012, at 18-19, available at http://www.delaneykester.com/files/enforcementmanual.pdf.

The SEC closes investigations with written reports. The same senior attorney in the SEC OGC explained: "When an investigation is closed, a closing recommendation and a closing report are generated." *Id.*, ¶ 6, Ex. 37. This was the procedure followed in 2013 if the MUI was closed. In sum, no matter how the SEC closed its investigation—whether as a MUI or an informal investigation—someone made a decision to stop it. That decision must be reported in one of two ways: on HUB or a CCR. In either case, the recommendations that resulted in closing the case should be treated as part of that report. The Enforcement Manual confirms that. Hence, the records of the closing—whether the notations on HUB or the CCR—should be released along with the CCR under *NLRB*, 421 U.S. 132.

IV. Abandoning Its *National Parks* Theory, the SEC Now Invites This Court to Take a Step No Ninth Circuit Court Has Ever Taken: Adopt *Critical Mass*

Edelman informed the Court the SEC has continuously reversed its contentions throughout the two years of administrative and judicial proceedings. Ds.17 at 2 and 23-1 at 8. The SEC has done so again. In its opening brief, it contended "The Ninth Circuit has never addressed or adopted the *Critical Mass* test, and *District courts in this circuit have adhered to the National Parks test* (emphasis added)." D. 22-1 at 8. It argued that it properly withheld various "confidential records" obtained from Malkin Holdings in reliance on *Nat'l Parks & Conservation Asso. v. Morton*, 498 F.2d 765 (D.C. Cir. 1974).

In his opposition, Edelman pointed out the SEC's legal and factual theory for withholding records under Exemption 4 conflicted with the Ninth Circuit's interpretation and application of *National Parks*. D. 23-1 at 21. The SEC apparently agrees, since it abandoned its argument based on Ninth Circuit decisions. It now asks this Court to adopt the District of Columbia Circuit Court's holding in *Critical Mass Energy Project v. Nuclear Regulatory Comm'n*, 975 F.2d 871 (D.C. Cir. 1992). This is not the first time the SEC has leapt from theory to theory during a summary judgment motion on Exemption 4. It did the same in *Aguirre v. SEC*, 551 F. Supp. 2d 33, 51-52 (D.D.C. 2008), prompting the Court to observe:

> Defendant has recently changed its position with respect to these documents, for until December 2007, the SEC took the position that the disclosure of these excerpts of deposition testimony would cause substantial harm to Pequot's competitive position, but now it invokes the impairment prong of Exemption 4 to support its withholdings.

No District Court in the Ninth Circuit has ever adopted or approved the theory of *Critical Mass* in the 25 years since it was decided. During those years, the Ninth Circuit has issued 16 decisions discussing Exemption 4, and the Ninth Circuit District Courts issued 57 decisions discussing same exemption. Aguirre Decl. ¶ 8. One way or another, none adopted or relied upon *Critical Mass.*

The District Court in *Dow Jones Co., Inc. v. F.E.R.C.*, 219 F.R.D. 167, 178 (C.D. Cal. 2003) sheds light why Ninth Circuit courts shied away from *Critical Mass*:

> Although defendant urges this Court to adopt Critical Mass, the Court believes that the holding therein is not consistent with Ninth Circuit jurisprudence, nor with the purposes of Congress in enacting FOIA, which mandates the courts to favor disclosure to serve the public interest. The Court also notes that the test set forth in Critical Mass has not been adopted by any Circuit other than the District of Columbia Circuit and has been the subject of criticism by some courts.

See also: *San Juan Citizens Alliance v. United States DOI*, 70 F. Supp. 3d 1214, 1219-1220 (D. Colo. 2014)("many courts have criticized the voluntary versus involuntary distinction made in *Critical Mass*.")

Further, *Critical Mass* only comes into play if records are voluntarily submitted to the agency. Even the D.C. Circuit courts have narrowed the reach of Critical Mass by broadly construing when records are involuntary submitted. *Pub. Citizen Health Research Grp. v. F.D.A.*, 964 F. Supp. 413, 414 n.1 (D.D.C. 1997)("Information is submitted involuntarily…if it is supplied pursuant to statute, regulation or some less formal mandate."); *Judicial Watch, Inc. v. U.S. Dep't of the Treasury*, 796 F. Supp. 2d 13, 35 n.8 (D.D.C. 2011)("For purposes of Exemption 4, information provided to the government because it is required for participation in a voluntary government program is treated as a mandatory,..."). In this case, Malkin Holdings voluntarily sought SEC approval for the ESRT IPO, which affected thousands of investors, including the 2,891 in

ESBA. The SEC made the request while the IPO was pending. It requested Malkin Holdings' records relating to an alleged fraud in connection with the pending IPO. The SEC could have suspended the IPO in a heartbeat. Without a doubt, Malkin Holdings' submittal of the records was involuntary under the case law cited above.

V. The SEC Has Outdone Itself on Its Assertion of Exemption 4 in Withholding the 97-Page Index of the Malkin Records

In its opening brief, the SEC specifically argued that "the parties have agreed that the defendant should move for summary judgment as to…" the 97-page index. D. 22-1 at 2, l. 16. Again, Edelman's opening brief demonstrated the SEC's assertion was groundless. Now, the SEC argues that the summary judgment motion does not cover the 97-page index. D. 25 at 3. The SEC cannot unilaterally withdraw its summary judgment motion when it decides the issue is not going its way. In any case, Edelman seeks summary judgment that both indexes should be released.

VI. The Ignores Its Duty to Segregate

Once again, the SEC has made no effort to segregate nonexempt material from the portion of records its claims is exempt. As the SEC knows, it is reversible error for the District Court "'to simply approve the withholding of an entire document without entering a finding on segregability, or the lack thereof, with respect to that document." *Hamdan v. U.S. DOJ*, 797 F.3d 759, 778-779 (9th Cir. 2015).

VII. Edelman Requests the court to Set Discovery

Edelman submits the SEC's groundless opposition and flip-flops in response to this motion point to the need for discovery. He requests the Court set the depositions of FOIA Specialist Luetkenhaus and Branch Chief McInerney and direct the SEC to release all writings generated by the FOIA Office relating to its efforts to comply with Edelman's FOIA requests.

DATED: February 28, 2017 Aguirre Law, APC

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