



is the sec's home court advantage coming to an end?

MSK Client Alert

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Defendants hauled before the Securities and Exchange Commission's administrative judges have long-suspected that the SEC enjoys a home-court advantage. An analysis by the Wall Street Journal found that, in the last five years, the SEC has prevailed in 90% of the cases in which it brought claims in its own administrative courts, but only in 69% of the cases when a federal court judge heard the claims.¹ Those type of odds are even more concerning for defendants given the expansion of the jurisdiction of administrative courts by the Dodd-Frank Act, which gave the SEC the power to seek penalties in administrative proceedings against even those individuals and companies it did not regulate.

However, the SEC's administrative courts have come under a barrage of legal attacks, and a recent court decision suggests that the SEC's ability to prosecute claims before its own judges may be curtailed. In June, a federal district court judge in Atlanta granted a preliminary injunction preventing the SEC from proceeding with an administrative hearing against the plaintiff. In that case, *Hill v. SEC*,² the plaintiff asked the federal district court to enjoin the SEC from pursuing an administrative hearing against the plaintiff on the ground that the administrative proceeding was unconstitutional. In particular, the plaintiff argued that the SEC administrative process: (1) violated Article I of the Constitution by delegating decision-making authority to the SEC to determine the forum to bring claims when such power is limited to Congress; (2) violated the Seventh Amendment right to a jury trial; and (3) violated the Article II Appointments Clause.

The federal district court rejected the first two arguments, but held that the plaintiff had established a likelihood of prevailing on the merits of his Appointments Clause claim because the SEC administrative law judge was an inferior officer that, under Article II, must be appointed by either the President, a court of law, or a department head. The administrative judge at issue had not been appointed by an SEC commissioner (the "head" of the department), thereby violating the Appointments Clause. The federal district court entered a

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preliminary injunction; it has not yet entered a final ruling, and the SEC has appealed to the Eleventh Circuit.

The ruling in *Hill* gives hope to opponents of the SEC administrative process, but it remains an outlier. Other plaintiffs have challenged the process in federal district court but have been unsuccessful. Several federal district courts have held that they do not have subject matter jurisdiction to rule on the constitutionality of the administrative process because Congress specified a method of judicial review: after the SEC judge and Commissioners rule on claims, their decision is subject to appeal to a federal court of appeals.³ At least one other federal district court found that it had subject matter jurisdiction, but rejected an initial constitutional challenge to the SEC administrative process.⁴

Moreover, as the court itself in *Hill* noted, the SEC can easily remedy the constitutional deficiency relied on in that case by having an SEC Commissioner, as "head" of the department, directly appoint the administrative law judges. Nevertheless, numerous additional challenges to the administrative court process continue to be filed, including several before the judge who decided the *Hill* case.⁵ Eventually, this issue will need to be determined by the federal courts of appeal, if not the United States Supreme Court. Until then, the *Hill* case gives hope to those looking to defend themselves in federal court.

1 Eaglesham, Jean, "SEC Wins With In-House Judges," *The Wall Street Journal*, May 6, 2015, available at <http://www.wsj.com/articles/sec-wins-with-in-house-judges-1430965803>

2 *Hill v. SEC*, 2015 U.S. Dist. LEXIS 74822 (N.D.Ga. June 8, 2015).

3 See *Tilton v. SEC*, 2015 U.S. Dist. LEXIS 85015 (S.D.N.Y. June 30, 2015); *Bebo v. SEC*, 2015 U.S. Dist. LEXIS 25660 (E. D. Wisc. March 3, 2015).

4 *Duka v. United States SEC*, 2015 U.S. Dist. LEXIS 49474 (S.D.N.Y. Apr. 15, 2015).

5 Beeson, Ed, "SEC Slapped With New Challenge To In-House Court," *Law360* (July 15, 2015), available at <http://www.law360.com/securities/articles/679501/sec-slapped-with-new-challenge-to-in-house-court>.