

## Critics Question SEC's Increasing Use of Administrative Enforcement Proceedings

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The **SEC is increasingly bringing enforcement actions** in its administrative forum rather than federal district court, **setting the stage for a legal and policy battle over this tactic**.

The SEC's approach has been made possible by a series of legislative enhancements to the agency's enforcement powers that began with the passage of the Securities Enforcement Remedies and Penny Stock Reform Act of 1990. The result of these enhancements has been to greatly expand the remedies available to the Commission in an administrative proceeding beyond [its traditional tool, the cease and desist order](#). The latest expansion occurred with the passage of the Dodd-Frank Act in 2010, which authorizes the Commission to seek civil money penalties against non-regulated persons or entities (*i.e.* not associated with investment advisors, brokerage firms, and other registered entities). Prior to Dodd-Frank, the SEC could file such actions only in federal court. This new enforcement authority gives the SEC a powerful incentive to bring more cases in the administrative forum.

Recently, SEC officials have signaled a tactical shift away from bringing cases in federal district courts. In June, SEC Director of Enforcement Andrew Ceresney told a D.C. Bar audience that the SEC will choose the administrative forum more often in insider trading and other cases. Just last month [Ceresney told the \*Wall Street Journal\*](#) that "[w]e're using administrative proceedings more extensively," while Kara Brockmeyer, head of the SEC's FCPA unit, described administrative proceedings as "the new normal."

Critics of the SEC's new tactics argue that the practice is unfair to respondents and possibly even unconstitutional. As a practical matter, SEC ALJs are employees of the Commission, and the first appeal from an ALJ decision is to the Commission itself. The system would appear to give the SEC a home-court advantage, an appearance that is borne out by the facts.

**In the twelve months ending September 2014, the SEC won 100% of contested administrative proceedings, but only 61% percent of federal court trials, according to the *Wall Street Journal*.**

Critics also argue that procedural protections for respondents in administrative proceedings are not nearly as robust as those in federal court:

- the rules allow only a few months to prepare a defense;
- they largely prohibit pretrial discovery and defense motions; and
- the federal rules of evidence do not apply, so hearsay evidence can be admitted.

Several cases have been filed recently that challenge the constitutionality of SEC administrative proceedings.

U.S. District Judge Jed Rakoff has been one of the most vocal critics of the SEC's new tactics. [In a recent opinion](#), he wrote: "[T]he Court of Appeals invites the SEC to avoid even the extremely modest review it leaves to the district court by proceeding on a solely administrative basis... One might wonder: from where does the constitutional warrant for such unchecked and unbalanced administrative power derive?" In a November 5, 2014 keynote address at the PLI Securities Regulation Institute, Rakoff argued that the primary fault in bringing cases administratively is that it hinders the development of the securities laws. Rakoff noted that most SEC enforcement actions are brought under the general anti-fraud provisions of the securities laws and that the development of the law under these catch-all provisions has been judge-made. If the SEC were to bring future cases in the administrative forum, "the law in such cases would effectively be made, not by neutral federal courts, but by SEC administrative judges." Rakoff cautioned that, although this tactic might result in short-term victories for the agency, it might not be good for the agency in the long run because the SEC should consider its own reputation for fairness and the development of securities law in general.

The SEC seems committed to bringing more enforcement cases as administrative proceedings. That said, it may also be considering at least some of the criticisms that have been made against its increased use of administrative proceedings. In June, SEC General Counsel Ann K. Small stated that it was fair for attorneys to question the SEC's rules for administrative proceedings, because they were last revised "some time ago" – before the passage of Dodd-Frank.

We will provide updates on this issue as they arise.

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