

Forum Selection In Contested Cases - The SEC Explains

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Earlier this month, after substantial criticism from defendants, practitioners, and even a federal judge, the SEC's Enforcement Division issued its first formal guidance explaining how it determines whether to bring an enforcement action in federal district court before the SEC's own administrative law judges. The Enforcement Division's "guidance" makes clear that it leaves itself with substantial discretion to decide the appropriate forum in which to bring a contested case. Just as interesting, however, is what the SEC does not say factors into that decision.

This post discusses some of the issues surrounding the SEC's forum selection issues. Part II will address the agency's just-published guidance to address those concerns.

By way of background, the SEC has long had the ability to choose the venue in which it brings an enforcement action, at least for some of its enforcement actions. Traditionally, the SEC employed its administrative proceedings for smaller actions, like books and records violations, against regulated entities, like broker-dealers. Administrative proceedings have both looser evidentiary standards, less permissive discovery (particularly depositions by defendants), and are subject to shorter time requirements (generally 300 days from the filing of proceedings to initial decision). With Dodd-Frank's enactment, though, Congress gave the SEC authority to bring in-house actions against additional persons and entities and to seek a broader array of potential remedies against them. For example, the SEC now can bring insider trading cases before its own ALJs. It is no secret that the Commission fares better before its own ALJs than it does in federal court. Last year, the agency won 100 percent of its administrative hearings while only winning 61 percent of its trials that year. It also seems that a noticeable uptick in the proportion of matters the Commission initiated on its own "home court" followed the SEC's high-profile defeats in federal court in 2013-2014 in several high-profile insider trading cases, including the Mark Cuban case, the Steffes case and the [Life Partners Holdings case](#). In fact, the Commission makes no bones about it. As SEC enforcement director stated several months ago, "[t]here is no question that we are using the administrative forum more often now than in past years, largely because of efficiency."

Come Under Fire

The increasing use of administrative tribunals has generated substantial criticism, including from Judge Jed Rakoff of the Southern District of New York. Judge Rakoff has spoken repeatedly about his hope that the agency will

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“think twice” and use its administrative proceedings sparingly in complex cases. He has expressed concern that ALJs may lack the objectivity and distance that federal judges have, despite their familiarity with the securities statutes, with potentially unintended consequences. Judge Rakoff has called it “troubling” that the “broad anti-fraud provisions, critical to the transparency of the securities markets, that have historically been construed and elaborated by the federal courts,” would be interpreted by ALJs ([particularly in ways that could then require deference from federal courts](#)). In at least three cases filed in federal court, parties have challenged the SEC’s use of administrative proceedings on various constitutional grounds, including due process. Thus far, these cases have gotten little traction. In its most recent filing in one of those cases, *Bebo v. SEC*, the agency argued to the Seventh Circuit that it lacked jurisdiction to review the defendant’s due process until after the administrative proceedings before the SEC had been completed and a final order issued by the agency. Nonetheless, these cases raise important due process issues about how even the playing field is in proceedings before the SEC, particularly in complex cases. Our upcoming post addresses the SEC’s guidance which responds to this criticism and some questions that remain open even after that guidance.