Supreme Court Plays Its Cards on Constitutionality of SEC In-House Court Actions

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The U.S. Supreme Court's June 2023 decision to grant certiorari in SEC v. Jarkesy called into question the SEC's ability to pursue penalties and other legal remedies before the SEC's in-house administrative law judges. If successful, this appeal could severely limit the SEC's ability to quickly resolve enforcement actions — SEC rules require that such administrative proceedings conclude within at most 120 days after post-hearing or dispositive motion briefing. In Jarkesy, the SEC brought suit before an ALJ in an administrative proceeding against George Jarkesy Jr. and his registered investment adviser, Patriot 28, for alleged securities fraud. Despite Jarkesy's demand for a jury trial (the rules for such proceedings do not provide for any jury trial), the ALJ continued with the action. Ultimately, the ALJ found Jarkesy liable and granted the SEC's request for equitable remedies and the imposition of civil penalties. The Seventh Amendment provides for the right to a jury trial for actions at law, but not for equitable actions. Historically, courts of law, rather than courts in equity, have enforced civil penalties. Consequently, when a plaintiff seeks civil penalties, the action is considered an action at law, attendant to which is the Seventh Amendment right to a jury trial. Thus, in accordance with the above reasoning, the Fifth Circuit Court of Appeals held that it was a violation of the defendants' Seventh Amendment right for the ALJ not to have allowed for a trial by jury. The SEC seeks to rely on the "public rights" exception to this general rule: when Congress, by statute, creates a "public right" and properly assigns the right to be adjudicated before ALJs, the Seventh Amendment does not require a trial by jury. This exception applies only where the use of a jury would disrupt the process Congress contemplated for resolution of the right, i.e., only if the right is so clearly integrated within a comprehensive regulatory scheme that the right is appropriately left for agency resolution. The Fifth Circuit found the "public rights" doctrine inapplicable under the circumstances. This is because (1) securities fraud actions reflect common law fraud actions, which are focused on redressing private harms, (2) jury trials of securities fraud actions would not "go far to dismantle the statutory scheme," and (3) securities fraud enforcement actions are "not uniquely suited for agency adjudication," as shown by the many decades worth of federal court enforcement actions alleging violations of federal securities laws and regulations. The grant of certiorari in *Jarkesy* comes on the heels of the Supreme Court's April 2023 decision in SEC v. Cochran, wherein the court held that defendants facing SEC claims in an administrative forum can challenge the ALJ's constitutional authority via an interlocutory appeal to the federal district courts. The highest court's decision is contrary to the long-standing policy of forcing defendants to wait until the conclusion of an administrative proceeding before a court may hear such an appeal on constitutional grounds. Cochran itself substantially undermined, as a practical matter, the SEC's ability to efficiently use administrative proceedings before ALJs. Cochran, moreover, may have tipped the Supreme Court's hand in Jarkesy, foreshadowing a constitutional limitation on the SEC's ability to use ALJs to swiftly resolve securities law claims. The Supreme Court's ultimate decision on the constitutionality of ALJs could have a broad impact on many types of agency administrative proceedings throughout the United States. Stay tuned to see who has a winning hand.

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