

Op-Ed: Welcome News from the SEC on Forum Selection

Details on choice of administrative versus court proceedings could help eliminate unfairness.

BY JOEL M. COHEN AND BENNETT RAWICKI

The U.S. Securities and Exchange Commission has taken an important step in responding to the debate over the proper use of its administrative proceedings. In the face of mounting pressure from lawsuits, public criticism and congressional concern, on May 8 the SEC's Division of Enforcement released an explanation of how it chooses between bringing an enforcement action in federal court and bringing it in an administrative proceeding.

The release, "Division of Enforcement Approach to Forum Selection in Contested Actions," identifies these considerations: the types of liability theories and forms of relief available in each forum; whether a defendant is a registered entity; the cost- and time-effectiveness of each forum; and whether the case presents complex securities law issues about



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which the SEC has more expertise.

By describing its considerations — although the division took care to note the list may not be exhaustive and did not limit its discretion — the SEC begins to answer the concern Sen. John Boozman, R-Arizona, recently expressed during SEC chairwoman

Mary Jo White's testimony to the Senate Appropriations Committee: the importance of "fairness and transparency" in the SEC's choice of forum.

Since the Dodd-Frank Act expanded the SEC's ability to impose monetary penalties in administrative proceedings, the

agency has increased its use of that forum and broadened the types of cases it brings administratively — most notably insider-trading cases. This increase has led to mounting criticism because defendants face significant disadvantages in administrative proceedings compared to federal court, including limited discovery, less time to prepare a defense, hearsay evidence and the absence of a jury.

These disadvantages are particularly problematic for defendants in insider-trading cases, or cases in which witnesses testify differently about key events, since the features designed to make administrative proceedings more efficient hinder defendants' ability to prepare a complete defense.

Facing these disadvantages, defendants in administrative proceedings have raised constitutional challenges to the SEC's choice of forum. One of the legal claims asserts that the SEC violates the Constitution's guarantee of equal protection when it sues one defendant administratively but others in federal court. The division's release responds to the equal-protection claim's key issue — whether the SEC had a legitimate, rational basis for treating the defendants differently by choosing different forums.

The division's release may affect both the pending litiga-

tion against the SEC and the continuing debate about the proper use of administrative proceedings. In the equal-protection claims against the SEC, the agency has never attempted to explain why it sued a particular defendant administratively.

Now that defendants have an explanation, they can search for inconsistencies in how the SEC applies the publicized considerations. An inconsistency can be evidence that the SEC violated equal protection by lacking a legitimate, rational basis for suing a particular defendant administratively but a similar one in federal court.

The division's release also increases the likelihood that defendants bringing equal-protection claims can receive discovery of the division's choice-of-forum decision. By publicizing its considerations for choosing a forum, the division weakened its argument that this decision-making must remain confidential, which means defendants can more easily overcome the SEC's assertions of the law-enforcement or deliberative-process privileges.

The greater effect of the release may be as a first step toward reforming administrative proceedings. Although the division's release focuses on the benefits of each forum to the SEC's litigation interests — provid-

ing little to assuage defendants' concerns about the fairness of administrative proceedings — by knowing the division's considerations, Congress and the public can better engage the agency on two important issues: first, which types of enforcement actions should be handled administratively; and second, whether administrative proceedings should offer defendants greater procedural protections, especially in the discovery area.

SEC director of enforcement Andrew Ceresney, in a speech to the New York City Bar Association on May 12, confirmed that he "hope[s] the public release will provide increased visibility into our thought process." The SEC's willingness to engage this issue may bode well for further dialogue in the continuing debate about securities law enforcement in the Dodd-Frank era.

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