

[Securities Regulation Daily Wrap Up, ENFORCEMENT—2d Cir.: ALJ challengers again taste defeat, \(Aug. 24, 2016\)](#)

Securities Regulation Daily Wrap Up

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By [John M. Jascob, J.D., LL.M.](#)

Challengers to the SEC's administrative enforcement regime have once again been thwarted by a federal appellate court. The Second Circuit has denied without comment petitions for rehearing or rehearing *en banc* filed separately by businesswoman Lynn Tilton and former Standard & Poor's executive Barbara Duka. Tilton and Duka had each sought to have the court reconsider rulings that a federal district court lacked subject matter jurisdiction over their constitutional attacks on the SEC's method for appointing administrative law judges ([Duka v. SEC](#); [Tilton v. SEC](#); August 23, 2016, *per curiam*).

Tilton's petition for rehearing. On June 1, a divided panel of the Second Circuit had [rejected](#) Tilton's attempt to enjoin an SEC administrative action charging her and several of her Patriarch Partners investment firms with fraud under the Advisers Act. Tilton asserted that the appointment of the SEC's administrative law judge violated the U.S. Constitution's Appointments Clause, and that she had the right to compel her constitutional arguments to be heard in the federal Southern District of New York. Siding with the district court, however, the two-judge majority concluded that Congress intended the SEC's administrative scheme to preclude district court jurisdiction and that the scheme encompasses an Appointments Clause challenge to a presiding ALJ.

In her [petition for rehearing](#), Tilton stressed that prohibiting targets of SEC administrative actions from raising constitutional challenges until after the proceedings have concluded compels respondents to defend themselves in front of unconstitutional ALJs. According to Tilton, the possibility of access to an appellate court only after losing in an administrative proceeding does not provide respondents with "meaningful review." Tilton also argued that the panel majority's decision conflicted with precedent and was irreconcilable with the Supreme Court's holding on "nearly indistinguishable" facts in *Free Enterprise Fund v. Public Company Accounting Oversight Board*.

Duka's petition. After *Tilton* was decided, the Second Circuit vacated a district court's order that halted the Commission's proceeding against Duka, a former manager at Standard & Poor's Rating Services whose handling of ratings for commercial mortgage backed securities allegedly violated SEC rules. The Southern District of New York had ruled that, based on Duka's complaint, the SEC's administrative law judges may have been appointed in violation of Article II. In light of *Tilton*, however, the Second Circuit [vacated](#) the district court's order and remanded the matter. As the Second Circuit's order was based exclusively on the decision in *Tilton*, Duka also moved for rehearing.

Duka [contended](#) that, under *Tilton*, she would be forced to: (1) defend herself before an unconstitutional ALJ; (2) in the event of an adverse ruling, incur sanctions and proceed through the SEC's glacial appellate process; (3) then raise an Appointments Clause challenge before a federal appellate court; and (4) upon prevailing on the merits, undergo a second proceeding that accords with the Appointments Clause. Citing Judge Droney's dissent in *Tilton*, Duka argued that this would not be "meaningful judicial review" under the established test for determining district court jurisdiction in the context of a statutory scheme that provides for judicial review of final agency actions. Duka also argued that the panel majority's ruling concerning the other two factors of the jurisdictional test—whether the challenge presented is "wholly collateral" to the administrative proceeding and whether "agency expertise" exists to address the specific claim—contravened precedent by rendering those factors devoid of substance.

String of defeats. The Second Circuit's orders denying Tilton's and Duka's petitions mark just the latest in a string of appellate defeats suffered by respondents attempting to block SEC enforcement proceedings on

constitutional grounds. On August 9, the D.C. Circuit [upheld](#) an SEC order barring Raymond J. Lucia and his advisory firm from the securities industry for misrepresenting their investment results. Lucia likewise argued that the SEC's decision was constitutionally infirm because the ALJ who presided over his case was an "officer" who was not appointed pursuant to the requirements of the Appointments Clause. The D.C. Circuit decided the Article II issue in the Commission's favor, however, finding that the ALJs were not inferior officers because the SEC's regime denies independent finality to their initial decisions.

The cases are [No. 15-2732](#) (*Duka*) and [No. 15-2103](#) (*Tilton*).

Attorneys: Daniel Goldman (Petrillo Klein & Boxer LLP) for Barbara Duka. Paul D. Clement (Bancroft PLLC) for Lynn Tilton. Jacob H. Stillman for the SEC.

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