

Securities Regulation Daily Wrap Up, ENFORCEMENT—S.D.N.Y.: Judge protests SEC gag rule while approving settlement, (Oct. 31, 2022)

Securities Regulation Daily Wrap Up

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While opining that the SEC's rule of barring settling defendants from denying liability may violate the Constitution, a federal judge nevertheless approved a settlement consistent with circuit precedent.

In a remarkable opinion approving the settlement of an SEC action, a federal judge in the Southern District of New York excoriated the agency's practice of imposing so-called gag orders on settling defendants. According to the opinion, the SEC's demand that defendants neither admit nor deny its allegations stands in tension with the unconstitutional conditions doctrine, the spirit of the First Amendment, and the country's tradition of protecting free expression. Nevertheless, the court approved the settlement at the parties' request and consistent with Second Circuit precedent ([SEC v. Moraes](#), October 28, 2022, Abrams, R.).

The opinion adds to some recent backlash against the SEC's policy—nearly alone among federal agencies—of requiring settling defendants and respondents to agree not to publicly refute the allegations against them. In 2019 a think tank sued the agency, claiming that it could not publish a book critical of the SEC because the author was bound by a gag order; the suit was [dismissed](#) for lack of standing. More recently, former Xerox CFO Barry Romeril unsuccessfully asked a court to void a 2003 consent decree where he had agreed to “no deny” language. According to Romeril, the language functioned as a prior restraint in violation of his First Amendment and due process rights. The Second Circuit [rejected](#) his appeal, reasoning in part that Romeril willingly agreed to waive his rights in consideration of settlement. The Supreme Court [denied](#) certiorari.

The father of the judge in the instant case represented Romeril on his petition for certiorari. In the opinion, the court emphasizes that the SEC and CFTC are alone among federal agencies in requiring lifetime gag orders from individuals. Although respondents and defendants are not required to settle SEC actions, approximately 98 percent of them do, according to a 2013 speech by then-Commissioner Luis Aguilar.

In September the SEC [charged](#) two executives of a family investment office, including the defendant, with insider trading. The [complaint](#) alleged the defendant learned that Dun & Bradstreet was going to be acquired and traded in Dun & Bradstreet options ahead the announcement, as well as tipped another trader. The defendant settled the SEC's charges, which meant agreeing to no-admit-no-deny language. Although the defendant did not challenge this gag order, the court spent nearly all nine pages of its opinion protesting the practice before reluctantly approving the settlement consistent with *Romeril*.

The court wrote that while defendants may waive their First Amendment rights, this “does not mean that the government should be in the business of demanding that they do so.” In the court's view, this practice conflicts with the unconstitutional conditions doctrine, which holds that the government cannot condition the conferral of a benefit on the surrender of a constitutional right, even if the government is not obligated to provide the benefit. Decisions of the Fourth, Sixth, and Ninth circuits have rejected settlements, plea agreements, and contracts conditioned upon waivers of First Amendment rights.

The no-admit-no-deny language also functions as a prior restraint on speech, denying the public the opportunity to scrutinize the SEC's enforcement practices. “Indeed, the very people who are arguably in the best position to know of governmental abuse ... are those who are muzzled by the provision from speaking out,” the court posits. While the *Romeril* court observed that consent decrees mean giving up something the parties might have won in litigation, there is no dispute that the SEC would not be entitled to a lifetime gag order if the case had proceeded to trial, regardless of the outcome.

Finally, the court called the provision “quintessential viewpoint discrimination” because it targets speech based on its content. In closing, the court asked, “What is the SEC so afraid of? Any criticism, apparently—or, rather, anything that may even ‘create the impression’ of criticism—of that governmental agency.”

The case is [No. 22-cv-8343](#).

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