

Reining in Administrative Proceedings:

SCOTUS Holds Federal District Courts Have Jurisdiction to Hear Constitutional Challenges to Administrative Proceedings Initiated by the SEC and FTC

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April 18, 2023

On April 14, 2023, the United States Supreme Court (the “Supreme Court”) unanimously held that federal district courts have jurisdiction to consider certain claims challenging the structure of administrative proceedings brought by the Securities and Exchange Commission (“SEC”) and Federal Trade Commission (“FTC”) without first going through the administrative appeals process. In *SEC v. Cochran* and *Axon Enterprise, Inc. v. FTC*, the parties alleged that the established review schemes for administrative proceedings were unconstitutional, but the district courts declined to exercise jurisdiction over the claims. The Supreme Court’s recent holding allows individuals and businesses, including Michelle Cochran (“Cochran”) and Axon Enterprise, Inc. (“Axon”), to raise structural challenges prior to “being hauled before an agency that [they] allege is unconstitutionally structured.” Ultimately, this ruling has the potential to impose further constitutional limitations on the structure and operation of administrative proceedings.

SEC v. Cochran

In *SEC v. Cochran*, the SEC initiated an administrative proceeding against Cochran, an accountant, for failing to comply with Public Company Accounting Oversight Board standards. Cochran sought to challenge the structure of the administrative proceeding in the United States District Court for the Northern District of Texas at the outset of the proceeding and before a final administrative adjudication. Specifically, Cochran argued that the administrative proceeding was unconstitutional because the Administrative Law Judge (“ALJ”) was improperly protected from removal by the president. It is well established that ALJs must be subject to removal at the direction of the president. This authority allows the president to ensure that all laws are faithfully executed. Cochran argues that the current statutory removal restriction, which provides ALJs with “for cause” removal protection, is unconstitutional.

The district court dismissed Cochran’s claim for a lack of subject-matter jurisdiction. The district court reasoned that the Securities Exchange Act of 1934 (the “Exchange Act”) stripped district courts of jurisdiction to hear challenges to SEC administrative proceedings by assigning the review of agency decisions to the federal courts of appeals.

During an *en banc* hearing, the United States Court of Appeals for the Fifth Circuit (the “Fifth Circuit”) reversed and held that the district court had subject-matter jurisdiction to hear Cochran’s claim. The Fifth Circuit opined that Congress did not intend for constitutional challenges, like the one brought by Cochran, to be heard exclusively by the federal courts of appeals.

Axon v. FTC

In *Axon v. FTC*, the FTC initiated an administrative proceeding due to antitrust concerns over a potential acquisition. Axon proceeded to file a lawsuit in the United States District Court for the District of Arizona and alleged, among other claims, that the FTC’s structure provided an improper insulation from the president. The district court dismissed Axon’s complaint and held that any constitutional challenges should first be raised within the administrative proceeding. Unlike *Cochran*, the United States Court of Appeals for the Ninth Circuit affirmed and held that Congress had barred jurisdiction in federal district courts.

SCOTUS: Federal District Courts Retain Jurisdiction to Hear Structural Claims

The Supreme Court held that the review schemes established in the Exchange Act and the Federal Trade Commission Act do not displace district court jurisdiction over structural claims.¹ The Supreme Court reached its decision by applying the so-called *Thunder Basin* factors articulated in *Thunder Basin Coal Co. v. Reich*, 510 U.S. 200 (1994). First, the Supreme Court found that precluding district court jurisdiction could foreclose all meaningful judicial review.² Second, it found that the claims were wholly collateral to the statute's review provisions.³ Third, it found that the claims challenging the constitutionality were "outside the [Commissions'] expertise."⁴ Thus, writing for the Supreme Court, Justice Elena Kagan concluded, "[e]ach of the three *Thunder Basin* factors signals that a district court has jurisdiction to adjudicate Axon's and Cochran's sweeping constitutional claims."⁵

Key Takeaways

This holding has the potential to reduce administrative power by placing constitutional limitations on the structure and operation of administrative agencies. A party may now promptly seek to address structural issues to a federal district court before being forced to litigate in an administrative proceeding and before a final agency order. If successful, this could save a party significant time and resources that would typically be required to respond to an administrative proceeding. As a result, the SEC and other administrative agencies could be inclined to file more claims in federal district courts to avoid the growing number of complexities associated with administrative proceedings and may be more selective in bringing claims that can be asserted only via administrative proceedings (e.g., 102(e) claims by the SEC).

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¹ Justice Clarence Thomas wrote a separate concurrence and Justice Neil Gorsuch wrote an opinion concurring in the judgment.

² *Axon Enters., Inc. v. FTC*, No. 21-86, and together with *SEC v. Cochran*, No. 21-1239, at *14.

³ *Id.*

⁴ *Id.* at *16.

⁵ *Id.* at *11.