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Release: Volume 45 No. 19

<u>SUPREME COURT HOLDS FEDERAL AGENCIES' ADJUDICATION OF CERTAIN CLAIMS IN-HOUSE UNCONSTITUTIONAL</u>

On June 27, 2024, the U.S. Supreme Court issued a ruling in the case of *SEC v. Jarkesy*. In its decision, the Court held that the Securities and Exchange Commission's ("SEC") practice of imposing civil penalties through in-house administrative law judges ("ALJs") in securities fraud cases violates a defendant's right to a jury trial under the Seventh Amendment of the U.S. Constitution. The *Jarkesy* decision requires that such cases instead be heard and decided in federal court before a jury. This ruling also may also have a significant impact on enforcement actions brought by other federal agencies, including the National Labor Relations Board ("NLRB"), in which civil penalties are sought.

In *Jarkesy*, the SEC brought a civil enforcement action against investment advisor George Jarkesy and his hedge fund, Patriot28, for securities fraud, seeking civil penalties and other remedies. The SEC pursued this matter through its internal administrative process, with an ALJ presiding over the case. The ALJ found Jarkesy guilty and imposed a $300,000 penalty, which was later upheld by the SEC Commissioners.

Jarkesy and Patriot28 challenged the SEC's decision, arguing that the in-house adjudication had violated their Seventh Amendment right to a jury trial. The case reached the Fifth Circuit Court of Appeals, which agreed with Jarkesy and vacated the SEC's order. The Fifth Circuit analyzed whether those parties had a right to a jury trial by comparing the statutory action at issue to analogous common law claims. Under this test, courts also consider whether the "public rights" exception to Article III of the U.S. Constitution applies.

The case was then appealed to the U.S. Supreme Court, which ultimately affirmed the Fifth Circuit's decision. The Supreme Court noted that an action under the SEC's antifraud provisions replicates the common law claim of fraud, which has traditionally been tried before a jury. The Court also found that the civil penalties sought by the SEC constituted a punitive remedy and must therefore be adjudicated in a court of law. In addition, the Court found that the SEC's claim did not fall under the public rights exception, which allows certain matters to be heard and decided by administrative agencies internally and without a jury.

Similar to the SEC, the NLRB hears unfair labor practice claims using in-house ALJs. However, most of the remedies traditionally sought in unfair labor practice cases – for example, backpay, reinstatement, bargaining orders, etc. – are equitable, rather than legal, in nature. Therefore, the NLRB may argue that cases seeking such remedies may be heard by an in-house ALJ without running afoul of *Jarkesy* or the Seventh Amendment. Under the NLRB's recent decision in *Thryv, Inc.*, however, the Board expanded its remedies to include consequential damages for all direct or foreseeable pecuniary harms. Parties seeking to undermine the NLRB's internal processes may argue that consequential damages are a legal remedy which, under *Jarkesy*, would necessitate a jury trial. The plaintiff in *Energy Transfer LP v. NLRB*, a case filed the same day the *Jarkesy* decision was issued, has already challenged the constitutionality of the NLRB's policy to have ALJs adjudicate cases in which consequential damages are sought.

Various other federal agencies are likely to be impacted by the *Jarkesy* decision as well. The Department of Labor, for example, may face similar constitutional challenges to its administrative process for adjudicating violations of the Fair Labor Standards Act.

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Dated. July 23, 2024

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