SEC Adopts Amendments to Rules of Practice for Administrative Proceedings

On July 13, 2016, the Securities and Exchange Commission ("SEC") adopted important amendments updating its rules of practice governing its administrative proceedings.[1] These changes concern, among other things, the timing of hearings in administrative proceedings, depositions, summary disposition, the contents of an answer, admissibility of evidence and expert disclosures and the procedure for appeals.[2] The amendments are intended to update the rules and introduce additional flexibility into administrative proceedings, while continuing to provide for the timely and efficient resolution of the proceedings. The amendments will become effective sixty days after publication in the Federal Register and will apply to all proceedings initiated on or after that date.[3]

These amendments are long-awaited changes to administrative proceedings. They come at a time when the SEC's administrative process faces a perception in the media that it is unfair for defendants. Last year, *The Wall Street Journal* reported that from October 2010 through March 2015, the SEC won 90% of its administrative proceedings, while in the same period the SEC prevailed in only 69% of the cases it brought in federal district court.[4] This brief memorandum provides an overview of some of the key changes.

I. Timing of Hearings

The SEC made three amendments to Rule 360,[5] which governs the filing of an initial decision by the hearing officer and the timing for the initial stages of an administrative proceeding. First, the "trigger date" for the time to file an initial decision is changed from the date of service of the order instituting proceeding ("OIP") to 30, 75 or 120 days from the date of completion of post-hearing or dispositive motion briefing, or a finding of a default.[6] Second, the amendments extend the length of the prehearing period from the current four months to a maximum of ten months for cases designated as 120-day proceedings, to a maximum of six months for 75-day cases, and to a maximum of four months for 30-day cases.[7] Third, the hearing officer can be granted an additional thirty days to issue an initial decision by certifying at least 30 days before deadline that extra time is needed.[8]

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[1] See *Amendments to the Commission's Rules of Practice,* Release No. 34-78319; File No. S7-18-15 (July 13, 2016) ("Amendments"), available at https://www.sec.gov/rules/final/2016/34-78319.pdf. In September 2015, the Commission proposed for comment amendments to its rules governing its administrative proceedings.

[2] *Id*.

[3] *Id*.

[4] Jean Eaglesham, SEC Wins With In-House Judges, WALL ST. J., May 6, 2015, available at http://www.wsj.com/articles/sec-wins-with-in-house-judges-1430965803.

[5] 17 CFR 201.360.

[6] Rule 360(a)(2)(i). The OPI designates whether the proceeding is a 30-day, 75-day, or 120-day proceeding. Proceedings in the 30- day category are typically is reserved for proceedings under Section 12(j) of the Exchange Act. Proceedings in the 75-day category typically involve "follow-on" proceedings following certain injunctions or criminal convictions. Proceedings in the 120-day category range from routine matters involving a single violation of the securities laws to matters involving, for example, multiple and distinct alleged violations, a particularly voluminous investigative record, or a complex set of factual allegations. *See* the Amendments, *supra* n. 1, at n.18, 13.

[7] Rule 360(a)(2)(ii).

[8] Rule 360(a)(3).

II. Depositions

Perhaps most importantly, amended Rule 233 now permits parties in 120-day proceedings the right to notice three depositions per side in single-respondent cases and five depositions per side in multi-respondent cases.[9] It also permits each side to request two additional depositions under an expedited procedure.[10] Depositions are limited to seven hours in length.[11] Depositions are not permitted in 30-day or 75-day proceedings.

III. Summary Disposition

Rule 250[12] currently provides that a party may move for summary disposition after a respondent's answer is filed and documents have been made available to the respondent. The amended rule provides that three types of dispositive motions may be filed at different stages of an administrative proceeding and sets forth the standards and procedures governing each type of motion. First, a party may make a motion for a ruling on the pleadings on one or more claims or defenses, no later than 14 days after a respondent's answer has been filed.[13] Second, any party may move for summary disposition on one or more claims or defenses after a respondent's answer has been filed.[14] Leave of the hearing officer is not required to file such a motion in 30-day and 75-day proceedings, but is required for 120-day proceedings. Third, following the division's presentation of its case in chief, any party may make a motion, asserting that it is entitled to a ruling as a matter of law on one or more claims or defenses.[15] Leave of the hearing officer is not required to file such a motion for any type of proceeding.

IV. Contents of an Answer

Rule 220[16] sets forth the requirements for filing answers to allegations in an OIP. The amended rule requires respondents to state in their answer whether they intend to assert any "reliance" defense and whether the respondent relied on the advice of counsel, accountants, auditors, or other professionals (e.g, compliance officers) in connection with any claim, violation alleged, or remedy sought. Failure to do so may be deemed a waiver.

V. Admissibility of Evidence

Rule 320[17] provides the standards for admissibility of evidence. Under the current rule, the Commission or hearing officer may receive relevant evidence and shall exclude all evidence that is irrelevant, immaterial, or unduly repetitious. The amended rule adds "unreliable" to the list of evidence that will be excluded. Hearsay evidence will continue to be evaluated on a case-by-case basis, and may be admitted if it is relevant, material and reliable.

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[9] Rule 233(a)(1)-(2).

[10] Rule 233(a)(3).

[11] Rule 233(j)(1).

[12] 17 CFR 201.250.

[13] Rule 250(a). This is analogous to Rules 12(b)(6) and 12(c) of the Federal Rules of Civil Procedure. *See* Fed.R.Civ.P. 12(b)(6) (failure to state a claim upon which relief can be granted); 12(c) (judgment on the pleadings).

[14] Rule 250(b)-(c). This is analogous to Federal Rule of Civil Procedure 56 (summary judgment).

[15] Rule 250(d). This is analogous to Federal Rule of Civil Procedure 50(a) (judgment as a matter of law).

[16] 17 CFR 201.220.

[17] 17 CFR 201.320.

Rule 235[18] was amended to allow parties, upon a motion, to introduce into evidence depositions taken pursuant to Rules 233 or 234, investigative testimony, and certain sworn declarations. The standard for granting such a motion focuses on the admissibility and relevance of the statement, the availability of the witness for the hearing, and the presumption favoring oral testimony of witnesses in an open hearing. This amendment, that might allow the SEC to introduce into evidence investigative testimony which has not been subject to cross examination, could be detrimental to respondents.

VI. Expert Disclosures

Rule 222(b)[19] provides that a party who intends to call an expert witness shall disclose information related to the expert's background, including qualifications, prior testimony, and publications. The amended rule requires each party who intends to call an expert witness to submit a statement of the expert's qualifications, a listing of other proceedings in which the expert has given expert testimony during the previous four years, and a list of publications authored or coauthored by the expert in the previous ten years.[20] Importantly, draft reports and disclosures and most communications between a party's attorney and the party's expert are protected from disclosure.[21]

VII. Appeals

Rule 410(b)[22] currently requires petitioners to set forth all the specific findings and conclusions of the initial decision to which exception is taken, and provides that an exception that is not stated in the notice may be deemed to have been waived by the petitioner. The amended rule requires petitioners to set forth only a summary statement of the issues presented for review and limits petitions to a mere three pages.

VIII. Conclusion

While the new amendments provide additional safeguards to respondents, they still fall short of the procedural safeguards afforded defendants in federal district court. It remains to be seen whether these amendments will impact the statistical disparity described above, but the new amendments represent meaningful developments for respondents in SEC administrative proceedings.

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If you have any questions about the issues addressed in this memorandum or if you would like a copy of any of the materials mentioned, please do not hesitate to call or email Bradley J. Bondi at 202.862.8910 or bbondi@cahill.com; Charles A. Gilman at 212.701.3403 or cgilman@cahill.com; Jon Mark at 212.701.3100 or jmark@cahill.com; John Schuster at 212.701.3323 or jschuster@cahill.com; Sara Ortiz at 212.701.3368 or sortiz@cahill.com; or Michael Wheatley at 202.862.8932 or mwheatley@cahill.com.

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[18] 17 CFR 201.235.

[19] 17 CFR 201.222.

[20] Rule 222(b)(2).

[21] Communications relating to compensation for the expert's study or testimony, identifying facts or data that the party's attorney provided and that the expert considered in forming the opinions to be expressed, or identifying assumptions that the party's attorney provided and that the expert relied on in forming the opinions to be expressed are not protected from disclosure.

[22] 17 CFR 201.410.