Article III and Seventh Amendment Challenges to SEC Administrative Proceedings After Dodd-Frank

Daniel P. Dwyer, Esquire
INTRODUCTION

This article considers whether Congress impermissibly encroached on Article III of and the Seventh Amendment to the United States Constitution when it passed Section 929P of 2012’s Dodd-Frank Act. Section 929P allows the SEC to pursue claims for monetary penalties against unregistered persons through administrative proceedings. Administrative proceedings against unregulated persons for monetary penalties are constitutional only when the fines and penalties are wholly “incidental to” and “necessary for” enforcement of the agency’s regulations. Monetary penalties that are punitive or retributive are more than incidental and necessary. Therefore, if 929P’s penalties are punitive or retributive, Congress unduly encroached on Article III and the Seventh Amendment when it enacted Section 929P.

This discussion has four parts. Section I describes the gradual expansion of the remedies and penalties available to the SEC between 1933 and 2010. Section II describes the challenges to the SEC’s administrative proceedings that currently appear to be most prevalent. These are facial challenges based on the separation of powers between the Legislative and Executive branches of the federal government. In effect, they question the constitutionality of Congress’ creation of Executive branch entities whose members the Executive cannot remove at will. This

* M.P.A., Univ. of Penna; J.D., Temple Univ. School of Law; B.A., Villanova Univ. This article was written as part of the author’s activities in the American Bar Association Business Law Section. The author is grateful for the invaluable assistance of Ryan Trifiletti, Esquire and Ms. Janine Chanoski.
Section concludes with a brief description of the limitations of the remedies provided by these facial challenges.

Section III describes a different separation of powers challenge to the SEC’s administrative proceedings. This challenge is based on the separation of powers between the Legislative and Judicial branches of government. It posits that Congress impermissibly encroached on the exclusive judicial powers and a litigant’s Seventh Amendment right to a jury trial when it created administrative bodies to pursue what are considered punitive, but not criminal, monetary penalties against unregistered persons. After describing the leading cases on Article III and Seventh Amendment jurisprudence of the last fifty years and the development of balancing tests for determining whether Congress impermissibly encroached on Article III and/or Seventh Amendment interests, the discussion turns to the Supreme Court’s 2011 decision in the case of *Stern v. Marshal*. This Section discusses why the balancing test developed in *Stern* should also be applied to questions regarding the use by the SEC of administrative proceedings against unregulated persons. Section IV is a brief conclusion.
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I. BACKGROUND: THE STEADY EXPANSION OF THE SEC’S TARGETS AND AVAILABLE REMEDIES PRIOR TO DODD-FRANK

A. 1934-1984: The SEC Pursues Equitable Relief in Article III Trials.

From its creation in 1934 until 1984, the focus of the SEC’s activities was remedial and focused on obtaining disgorgement and other injunctive orders from the United States District Courts.¹ The SEC’s primary activities consisted of rulemaking, obtaining cease-and-desist orders for unlawful conduct, barring violators from the securities markets, and obtaining disgorgement of ill-gotten gains in some cases.² Punitive measures were pursued by the Department of Justice in criminal actions also brought in the United States District Courts.³

The enforcement of the securities laws has never been limited to governmental enforcement; there has always been an element of private enforcement and rights of action. The Securities Act of 1933 expressly provided a private right of action against signers of registration statements that included material misrepresentations or omission.⁴ The Securities Exchange Act of 1934 also included a private right of action allowing investors to sue for manipulation or deception, insider trader profits, and false or misleading statements.⁵ Since 1946, the courts have recognized a private right of action under Rule 10(b) of the Securities Exchange Act of 1934 for violations of the use or employment of “any manipulative or deceptive device or contrivance in

² Barbara Black, Should The SEC Be A Collection Agency For Defrauded Investors, 63 BUS.LAW. 317, 322 (2008).
³ Atkins, Bondi, supra n.1 at 384.
contravention of such rules and regulations as the Commission may prescribe in connection with
the purchase or sale of any security registered on a national securities exchange or any security
not so registered, or any securities-based swap agreement.” 6 The SEC’s role in enforcing the
securities laws has never been exclusive.

B. 1984-1988: The SEC Obtains Authority to Pursue Monetary Civil
Penalties from Regulated Person and Inside Traders in Federal Jury Trials

With the passage of the Insider Trader Sanctions Act of 1984, the SEC was empowered
to pursue civil monetary penalties of up to three times the profit realized or the loss avoided as a
result of insider trading in United States District Court proceedings. 7 This authority was
increased four years later with the passage of the Insider Trading and Securities Fraud Act of
1988 which permitted the SEC to recover monetary penalties, through a jury trial in the United


throughout 15 U.S.C.). Section 2 of the 1984 Act provides:

Section 21 of the Securities Exchange Act of 1934 is amended by … adding at
the end thereof the following new paragraph: "… Whenever it shall appear to the
Commission that any person has violated any provision of this title or the rules or
regulations thereunder by purchasing or selling a security while in possession of
material nonpublic information … the Commission may bring an action in a
United States district court to seek … a civil penalty to be paid by such person, or
any person aiding and abetting the violation of such person. The amount of such
penalty shall be determined by the court in light of the facts and circumstances,
but shall not exceed three times the profit gained or loss avoided as a result of
such unlawful purchase or sale, and shall be payable into the Treasury of the
United States.

States District Courts, from controlling persons of those who trade on material non-public information in violation of the law. Although the 1984 and 1988 statutes showed a significant change in the SEC’s mission and available remedies, those remedies were only available through a jury trial in a district court. The 1988 Act also includes a private right of action for investors.

C. **1990: The Remedies Act Allows the SEC to Pursue Disgorgement Claims Against Regulated Persons in Administrative Proceedings.**

In 1990, Congress again increased the SEC’s remedies when it passed the Securities Enforcement Remedies and Penny Stock Reform Act of 1990 (“the Remedies Act”). Three sections of the Remedies Act allowed the SEC to recover monetary penalties from registered persons for violations of the securities laws through Article I administrative proceedings. These were: 1) Section 202, providing for administrative proceedings and monetary penalties against inside traders; 2) Section 301, providing for administrative proceedings and monetary penalties against persons barred from or otherwise ineligible to serve as underwriters, broker-dealers,

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9 Section 5 included a private right of action for certain investors against violators:

Any person who violates any provision of this title or the rules or regulations thereunder by purchasing or selling a security while in possession of material, nonpublic information shall be liable in an action in any court of competent jurisdiction to any person who, contemporaneously with the purchase or sale of securities that is the subject of such violation, has purchased (where such violation is based on a sale of securities) or sold (where such violation is based on a purchase of securities) securities of the same class.


investment advisors and related forms of investment professions other officer and director bars; and 3) Section 401 providing for administrative remedies against certain investment advisors for registration violations.\footnote{Remedies Act § 202(amending 15 U.S.C. §78u-1); § 301(amending 15 U.S.C. §80a-9); §401(amending 15 U.S.C. §80b-3).}

The Remedies Act also provided a new regimen for calculating monetary penalties. Each of the sections described above included a three-tier system for assessing monetary penalties that ranged from $5,000 per violation for a natural person and $50,000 per violation for any other person on the first tier to $50,000 per violation for a natural person and $500,000 for each violation for any other person on the third tier.\footnote{Id.} Disgorgement was provided as an alternate administrative remedy whereas prior to the enactment of the Remedies Act, the SEC could only obtain a disgorgement order by obtaining injunctive relief in the United States District Court.\footnote{Spehr, n.10, supra at 590; see also, Remedies Act §102(e)(codified as amended at 15 U.S.C. § 80a-9(e)) ("In any proceeding in which the Commission may impose a penalty under this section, the Commission may enter an order requiring accounting and disgorgement … ")} The third tier of highest penalties had a subjective element because it could be reached if the SEC determined that the violator’s actions caused “substantial losses or created a significant risk of losses to others.”\footnote{Remedies Act § 202(amending 15 U.S.C. §78u-1); § 301(amending 15 U.S.C. §80a-9); §401(amending 15 U.S.C. §80b-3).} Furthermore, the Remedies Act gave the SEC further latitude by allowing it to calculate penalties on the basis of the “gross amount of pecuniary gain” rather than the investors’ losses.\footnote{Remedies Act §201(4).}
The other four provisions of the Remedies Act allowed to pursue SEC monetary penalties from “any person,” not merely those who were registered with the SEC, through United States District Courts proceedings. These sections were: 1) Section 101 providing monetary penalties to be assessed against any person for violating the Securities Act of 1934; 2) Section 201 providing monetary penalties against officers and directors accused of insider trading; 3) Section 302 providing monetary penalties against any person accused of violating the Investment Company Act of 1940; and 4) Section 402 providing monetary penalties against investment advisors accused of making certain unlawful representations to the public.\textsuperscript{16} The Remedies Act specifically limited the SEC’s administrative jurisdiction to claims against directly regulated persons and inside traders. Article III remedies remained for unregulated persons.\textsuperscript{17}

\textbf{D. 2002: Sarbanes-Oxley Changes the SEC’s Mission and Increases the Amount of Penalties Pursued in Administrative Proceedings}

The SEC’s powers continued to expand with the passage of the Sarbanes-Oxley Act of 2002.\textsuperscript{18} The Sarbanes-Oxley amendments to the securities laws permitted the SEC to pursue officer and director bars in its own administrative courts.\textsuperscript{19} More importantly, Sarbanes-Oxley gave the SEC authority to pursue monetary penalties, in the form of “Fair Funds” to recompense defrauded shareholders for their losses.


\textsuperscript{17} Atkins, Bondi, n.1 supra. at 394.


\textsuperscript{19} Spehr, n.10 supra at 600.
The Fair Funds provisions reflected a significant change in the SEC’s mission.\textsuperscript{20} As described above, the SEC’s mission, prior to 2002, did not include recovering funds for defrauded investors. In 1968, Commissioner Richard P. Smith publicly stated that, “the Commission attempts to avoid being a collection agency for injured investors.”\textsuperscript{21} The Fair Funds provisions of Sarbanes-Oxley reversed this policy by providing for the recovery of funds for investors’ benefit. Section 308 provides that:

If in any judicial or administrative action ... the Commission obtains an order requiring disgorgement against any person ..., or such person agrees in settlement of any such action to such disgorgement, and the Commission also obtains ... a civil penalty against such person, the amount of the civil penalty shall, on the motion or at the direction of the Commission, be added to and become part of the disgorgement fund for the benefit of the victims of such violation. \textsuperscript{22}

The statute states two conditions for the creation of a fund for repaying investors: disgorgement by a violator and a civil penalty paid by the same violator. Sarbanes-Oxley also provided the SEC with broad authority to pursue “any equitable relief that may be appropriate or necessary for the benefit of investors ...”, regardless of whether the relief was construed as disgorgement or restitution.\textsuperscript{23} The Fair Funds provisions allow the SEC to elect the higher of either the violator’s


\textsuperscript{22} Sarbanes-Oxley Act §308 (emphasis added).

\textsuperscript{23} Spehr, n.10 supra at at 599 n.40 (\textit{citing}, Sarbanes-Oxley Act § 308).
gain or the investor’s loss to calculate the penalty or increase the available penalty. So although Sarbanes-Oxley did not increase the amount of the penalties tiers provided by the Remedies Act, the different methods it provided to the SEC for calculating and pursuing monetary penalties caused the amount of penalties recoverable thorough administrative proceedings to increase significantly.

E. 2010: Section 929P of the Dodd-Frank Act

In 2010, the Dodd-Frank Act further amended the various securities statutes. In particular, Section 929P increases the monetary penalties that the SEC can recover and broadens the class of persons from whom it can recover them. Section 929P(a)(1) amends Section 8A of the Securities Act of 1933 by permitting the SEC to pursue monetary penalties against violators of this Act though its administrative proceedings. These penalties can vary from $7,500 and $150,000 per violation for a natural person to between $75,000 and $725,000 per violation for all other persons. Section 929P(a)(2), (a)(3) and (a)(4) also permit the SEC to recover monetary penalties in its administrative proceedings for violations of the Securities Exchange Acts of 1934, Investment Company Act of 1940, and the Investment Advisors Act of 1940. The SEC

24 Atkins, Bondi, n.1 supra at 399; see also, Steinway, n.20 supra at 221. Because securities fraud is a highly inefficient form of crime with potentially vast disparities between victims’ losses and violators’ gain, allowing the SEC to choose between the two increases the recoverable damages. Urska Velikonja, The Cost of Securities Fraud, 54 WM.&MARY. L.REV. 1887 (2013).
27 Dodd-Frank § 929P(a)(1)(codified at 15 U.S.C. 77h-1(g)(1)).
29 Dodd-Frank § 929P(a)(2)(3).
can sometimes pursue penalties in excess of these amounts as a result of target eagerness to resolve claims, the Sarbanes-Oxley Act’s emphasis on shareholder recovery, and the provisions of the Remedies Act that provide the SEC with alternative methods to calculate and increase penalties.\(^{30}\) Moving these actions to an administrative forum with more deferential Article III oversight only increases the chance that targets will be exposed to greater damages.\(^{31}\)

**II. CHALLENGES TO THE SEC’S ADMINISTRATIVE PROCEEDINGS BASED ON THE SEPARATION OF POWERS BETWEEN CONGRESS AND THE EXECUTIVE BRANCH**

Not surprisingly, the unregulated persons, particularly officers and directors, object to being subject to these administrative proceedings and the increased damages and limited procedural protections they afford. An early challenge to some related Dodd-Frank changes was based on the separations of powers between the Congress and the Executive. This challenge, subsequent related challenges, and their possible limitations are discussed below.

**A. Free Enterprise Fund: A Limited Declaratory Judgment Challenge to Administrative Proceedings Based on the Separation of Powers Between Congress and the Executive**

Since the expansion of the jurisdiction of and remedies available in the SEC’s administrative courts, many respondents in SEC administrative proceedings have brought declaratory judgment actions challenging either the constitutionality of the SEC’s administrative courts or specific aspects of the proceedings or, more often, a combination of the two. These cases often rely on the Supreme Court’s decision in *Free Enterprise Fund v. Public Co. Accounting Oversight Bd.*\(^{32}\) In *Free Enterprise Fund*, a public accounting company challenged

\(^{30}\) Atkins, Bondi, n.1 supra at 398-99.


\(^{32}\) See n. 39 infra.
whether the Public Company Accounting Oversight Board (“PCAOB”), a new agency created by the Sarbanes-Oxley Act and placed under the supervision of the SEC, contravened the separation of powers doctrine.\textsuperscript{33} The challenge asserted that Congress unlawfully encroached upon the President’s Article II powers by using its Article I powers to create officers, both the PCAOB board members and the SEC commissioners, that the President could not remove at will.\textsuperscript{34} The Supreme Court held that declaratory relief was appropriate because: 1) the challenge was collateral to the Board’s decisions, and 2) the Board did not have the competency to address constitutional challenges.\textsuperscript{35} The Supreme Court also held that the tenure provided to both the SEC Commissioners and members of the PCAOB impermissibly restricted the President’s ability to remove them and thus violated the separations of powers between the Executive and Legislative branches.\textsuperscript{36} This, however, was a limited victory.

The remedy provided by the Court was not a finding that the Board’s existence was unlawful or a nullification of its acts or an injunction prohibiting it from acting. Rather, because the tenure provisions were severable from the statutory sections regarding the Board’s operations, the Court merely remanded the case with instructions to construe the statute as requiring that the PCAOB members be removable at will.\textsuperscript{37} Declaratory relief was awarded but injunctive relief was not.\textsuperscript{38} Although the separations of powers doctrine provided a valid basis

\textsuperscript{34} Free Enterprise Fund, 561 U.S. at 493.
\textsuperscript{35} Free Enterprise Fund, 561 U.S. at 506-07.
\textsuperscript{36} Free Enterprise Fund, 561 U.S. at 493.
\textsuperscript{37} Free Enterprise Fund, 561 U.S. at 493.
\textsuperscript{38} Free Enterprise Fund, 561 U.S. at 508.
for declaratory relief, challenges based on the separations of powers between Congress and the President based on tenure may not necessarily provide a meaningful remedy.

**B. Challenges to the SEC’s Administrative Proceedings Based on Free Enterprise Fund**

Since 2011, many respondents in SEC administrative actions have brought declaratory judgment actions challenging the SEC’s administrative jurisdiction on the basis of the separation of powers between Congress and the Executive addressed in *Free Enterprise Fund*. These challenges have enjoyed limited success. In four of these seven challenges, *Stilwell*, *Altman*, *Jaresky* and *Chau*, the District Courts (the Southern District of New York in all but one case) granted 12(b)(6) or other forms of motions to dismiss in declaratory judgment cases challenging the SEC’s acts or jurisdiction. The courts held that the declaratory judgment actions were

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challenges to specific acts of the administrative agency and so could first be adjudicated before
the SEC and an appeal could be reviewed by the Court of Appeals.\(^\text{40}\) Broader due process and
equal protection claims were rejected as non-specific or adjudicable by the administrative court
and reviewable by the Court of Appeals.\(^\text{41}\)

In the cases where equal protection claims were found to constitute a valid district court
challenge to the SEC proceedings, the specific facts regarding how the plaintiff was actually
harmed as a result of specific differential treatment by the SEC had to be alleged.\(^\text{42}\) Therefore,
although some constitutional claims and defenses may be asserted though declaratory judgment
actions filed in district courts, if the challenge is to the agency’s specific acts, courts will often
derfer such challenges to the administrative process. Further, and as \emph{Free Enterprise Fund}
showed, Courts will endeavor to find a remedy that keeps Congress’ action intact and which may
provide little relief to even a successful challenger.\(^\text{43}\)

\(^{40}\) \emph{Altman}, 768 F.Supp.2d at 560-61; \emph{Jaresky} 2014 WL 2584403 at *4; \emph{Chau}, 2014 WL 6984236 at **8-9.
\(^{41}\) Id.
\(^{42}\) \emph{See Gupta v. Securities and Exchange Comm.}, 796 F.Supp.2d at 514(where Gupta alleged that that all
other 28 defendants in insider trading cases related to the conduct of Galleon Management were the
subject of district court litigation and only plaintiff was pursued administratively, he stated an equal
protection claim); \emph{Altman}, 768 F.Supp.2d at 561-62(although equal protection claim based on assertion
treated similarly situated investment brokers differently based on their size or market share support a
valid collateral challenge to SEC jurisdiction which could be raised in district court in a declaratory
judgment action, in this case the allegations were insufficient specific to state a claim).
\(^{43}\) A recent case shows how the SEC might actually resist these judicial attempts at accommodation. \emph{Duka}
v. \emph{U.S. Securities and Exchange Comm.}, U.S.D.C., S.D.N.Y. No. 15-CV-857 is a declaratory judgment
action challenging an SEC administrative proceeding on the grounds that the SEC’s method of
appointment of Administrative Law Judges contravenes the appointments clause of Article II of the
Constitution. The United States District Court reserved judgment on Duka’s Petition for a Preliminary
Injunction for 7 days to permit the SEC to cure any violation of the Appointments Clause. Judge
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Unease about the SEC’s expanded use of administrative proceedings continues.\(^{44}\) The question is whether a theory other than that used in *Free Enterprise Fund* might make for a stronger declaratory judgment challenge and more appropriate remedy. A possible theory and remedy may be found in a separations of powers challenge based on the separation not between Congress (Article I) and the Executive Branch (Article II), but rather on the separation between Congress (Article I) and the Judiciary (Article III) as well as the jury trial protection of the Seventh Amendment.

The creation of Article I adjudicative bodies, be they courts or agencies, gives rise to a tension between Congress and its ability to propagate and enforce regulations, on one hand, and Article III and Seventh Amendment interests on the other. This is particularly true when regulatory and administrative penalties start to resemble those traditionally adjudicated by

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Berman’s Decision can be found at [http://www.nysd.uscourts.gov/cases/show.php?db=special&id=477](http://www.nysd.uscourts.gov/cases/show.php?db=special&id=477). On August 10, 2015, the Department of Justice informed the Judge Berman that the Commission decided not to reappoint the ALJs, as Judge Berman suggested, because the ALJs could determine the jurisdictional/constitutional question in its administrative proceedings, or the Commission could take the appointments question up at another time. Putting aside the question of whether the SEC’s administrative courts are competent to rule on such jurisdictional and constitutional questions (which, perhaps, one should not put aside too quickly, see *Petruska v. Gannon Univ.*, 462 F.3d 294, 304 (3d Cir. 2006)(“… as a general rule, an administrative agency is not competent to determine constitutional issues.”)), the SEC intends to keep fighting these Article II challenges, even when a remedy to any constitutional challenge is readily available.

Article III courts in jury trials. The following cases illustrate how courts have struggled with reconciling deference to Congress with protection of Article III and Seventh Amendment rights since the advent of the New Deal through the present day. This discussion begins with consideration of the language of and interest protected by Article III and the Seventh Amendment.

A. The Terms of Article III and the Seventh Amendment

Article III provides:

Section 1.
The judicial power of the United States, shall be vested in one Supreme Court, and in such inferior courts as the Congress may from time to time ordain and establish. The judges, both of the supreme and inferior courts, shall hold their offices during good behaviour, and shall, at stated times, receive for their services, a compensation, which shall not be diminished during their continuance in office.

Section 2.
The judicial power shall extend to all cases, in law and equity, arising under this Constitution, the laws of the United States, and treaties made, or which shall be made, under their authority … --to all cases of admiralty and maritime jurisdiction …

Article III serves two purposes: 1) to define the judiciary’s authority in the United States’ tripartite government in which it provides the courts with broad jurisdiction, and 2) to protect litigants in cases arising at law or in equity by assuring an impartial adjudicator who is not affected by the other governmental branches.

The Seventh Amendment provides:

In suits at common law, where the value in controversy shall exceed twenty dollars, the right of trial by jury shall be preserved, and no fact

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tried by a jury, shall be otherwise reexamined in any court of the United States, than according to the rules of the common law.\textsuperscript{47}

This is a different interest than that which is protected by Article III. While Article III protects the courts and litigants from other branches, the Seventh Amendment provides litigants with a jury trial to protect them from the judiciary in “suits at common law.”\textsuperscript{48}

\textbf{B. The Development Of Article III Separation of Powers Jurisprudence and the Seventh Amendment}

Although the interests protected by and the analyses applied to Article III and the Seventh Amendment have merged in recent years, historically, two different modes of analysis developed for addressing these questions. The authority of an Article III court to adjudicate a matter was analyzed in terms of whether the right at issue was a private right, which Congress could not remove from the courts, or a public right, which could be adjudicated by administrative tribunals. Public rights are those “which arose between the government and a person subject to its authority in connection with the performance of the constitutional functions of the executive or legislative departments.”\textsuperscript{49} Private rights are those involved in “the liability of one individual to another under the law as defined.”\textsuperscript{50}

The Seventh Amendment right to a jury trial for “suits at common law” compelled courts to look to whether the English common law as of 1791 provided a jury trial for a given claim.\textsuperscript{51}

\textsuperscript{47} U.S. Const., Seventh Amendment.

\textsuperscript{48} Sun, n. 46 \textit{supra} at 554-55.


\textsuperscript{50} \textit{Id}.

The Seventh Amendment right to a jury trial is also applied to claims which may not have existed in England as of 1791 but which are analogous to claims that existed at that time.\textsuperscript{52}

1. Public Rights Analysis for Questions Regarding the Separation of Powers Between Congress and the Judiciary

Although the definition of what constitutes a public right is easily stated, it is not so easily applied. This is because the breadth of Congress’ ability to implement legislative schemes to address societal conditions results in the creation of Article I administrative bodies, like the SEC, that adjudicate matters and disputes which, prior to the passage of the legislation, were either: 1) matters of private right, or 2) matters which, although newly created by Congress, are analogous to pre-existing private rights. Therefore, before considering the Court’s most recent ruling on the private right/public right Article III question, it is worthwhile to consider the precedents on which that decision relies.


Much of the modern discussion of public and private rights for purposes of separation of powers question begins with the Supreme Court’s 1932 decision in \textit{Crowell v. Benson}.\textsuperscript{53} \textit{Crowell} was an employer’s challenge to the constitutionality of a federal statute that created a workmen’s compensation scheme for longshoremen and harbor workers.\textsuperscript{54} The employer challenged the statute under the due process clauses of the 5\textsuperscript{th} and 14\textsuperscript{th} Amendments, Article III, the Seventh Amendment, the inapplicability of certain evidentiary rules, the use of an Article I Deputy Commissioner to adjudicate claims, and the standard of review applied to the Deputy

\textsuperscript{54} Crowell, 285 U.S. at 37.
Commissioner’s factual and legal findings.\textsuperscript{55} The Supreme Court easily disposed of the due process claims by applying the minimal standards for notice and hearing required to satisfy a due process challenge.\textsuperscript{56} The Seventh Amendment challenge was also disposed of with the observation that this was a matter of admiralty and maritime law that provided no right to a jury trial.\textsuperscript{57}

The Court then addressed the separations of powers issues, \textit{i.e.}, the ability of Congress to delegate the adjudication of these employee injury claims to executive officers like the deputy commissioner. Congress’ ability to delegate the adjudication hinged on whether the issue was a matter of public right, \textit{i.e.}, one that “arise[s] between the government and persons subject to its authority in connection with the performance of the constitutional functions of the executive or legislative departments” or a matter of private right involving the “liability of one individual to another under the law as defined.”\textsuperscript{58} If the matter was one of public right, Congress could delegate it to an Article I body.\textsuperscript{59}

Although \textit{Crowell} was a matter of private right in that it involved the liability of the employer to the employee for compensation, it was one that arose under the courts’ admiralty jurisdiction, and so the use of special masters and other administrative and adjudicators was permissible.\textsuperscript{60} However, to assure an Article III check on the Article I tribunals’ activities,

\begin{itemize}
\item \textsuperscript{55} \textit{Id.}
\item \textsuperscript{56} \textit{Crowell}, 285 U.S. at 46.
\item \textsuperscript{57} \textit{Crowell}, 285 U.S. at 45.
\item \textsuperscript{58} \textit{Crowell}, 285 U.S. at 50-51.
\item \textsuperscript{59} \textit{Id.}
\item \textsuperscript{60} \textit{Crowell}, 285 U.S. at 53. The Court also observed that had Crowell been a matter that arose under common, rather than admiralty, law, the use of a jury for fact-finding would “not only be deemed appropriate, but is required by the Constitution itself.” 285 U.S. at 51.
\end{itemize}
jurisdictional facts, those “precedent to the application of the statutory scheme” would be subjected to a de novo standard of review by a United States District Court. Thus, the Court upheld the District Court’s de novo review and reversal of the Deputy Commissioner’s findings while also upholding the overall statutory scheme that permitted involved Article I adjudications of matters of private right. To summarize, although Crowell is often cited as authority for the inapplicability of the Seventh Amendment to administrative actions, it actually tells us little about that question: because it was an admiralty case, there was no question of the application of the Seventh Amendment.

b. 1982: Northern Pipeline and The Zenith of Public Rights/Private Rights Analysis in Article III Analysis

Fifty years later, the Supreme Court again addressed the ability of congressionally-created bodies in Northern Pipeline Construction Co. v. Marathon Pipe Line Co. In Northern Pipeline, a creditor against whom a debtor asserted claims for breach of contract and breach of warranty challenged the provisions of the Bankruptcy Act of 1978 that permitted these claims to be adjudicated in the United States Bankruptcy Courts formed by Congress pursuant to its Article I powers. To determine whether these claims were properly before an Article I body, Justice Brennan identified “three narrow situations … each recognizing a circumstance in which the grant of power to the Legislative and Executive Branches was historically so exceptional that the congressional assertion of a power to create legislative courts was consistent with, rather than threatening to, the constitutional mandate of separation of powers.” These “narrow

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61 Crowell, 285 U.S. at 50-51. The separate standard of review for review for jurisdictional facts was disposed of five years later. See, St. Joseph Stockyards Co. v. United States, 298 U.S. 38, 53 (1936).
63 Northern Pipeline, 458 U.S. at 57
64 Northern Pipeline, 458 U.S. at 64.
situations” were: 1) territorial disputes in which no State acted as the sovereign; 2) question of military discipline (courts martial); and 3) issues involving public rights, as discussed in Crowell. Because Northern Pipeline clearly did not present any territorial or martial issues, Justice Brennan continued to consider what constitutes a public right and whether it could be applied to require an Article I bankruptcy court’s adjudication of these common law claims.

Justice Brennan did not definitively identify the distinction between public and private rights. However, he did state that public rights “must, at a minimum arise between the government and others” while private rights are those which arise out of “the liability of one individual to another under the law as defined.” Justice Brennan continued to observe that there was no “exceptional grant of power” to Congress to create a new court to adjudicate a breach of contract matter between two private parties; although Congress’ passage of the Bankruptcy Reform Act and the new Bankruptcy Code was such an “exceptional grant of power” to adjudicate the restructuring and discharge that is at the heart of bankruptcy proceedings, the matters of private right were not within that grant. In the absence of such a grant, the Court affirmed the District Court’s dismissal of the proceedings before the bankruptcy court. However, the Court’s remedy did not invalidate any of the Bankruptcy Court’s actions; rather, it merely stayed the judgment until Congress could rectify the inappropriate use of jurisdiction.

65 Northern Pipeline, 458 U.S. at 64-68.
66 Northern Pipeline, 458 U.S. at 69-70.
67 Id.
68 Id.
69 Id.
70 Northern Pipeline, 458 U.S. at 88.
In addition to considering the right being adjudicated, the plurality opinion in *Northern Pipeline* also considered the types of judicial adjuncts to which adjudications could be delegated. Justice Brennan rejected *Crowell’s* suggestion that the different types of adjuncts should be distinguished based on whether they are an Article I court or an administrative agency and, instead, evaluated the adjunct based on the type of claims it adjudicated. The plurality identified two types of adjuncts using this analysis: 1) those that adjudicate congressionally created public rights, and 2) those that assist the Article III courts in adjudicating rights that were not created by Congress, *e.g.*, constitutional or private right claims. Private right claims could not be adjudicated by the first type of adjunct without creating “substantial inroads into functions that have traditionally been performed by the Judiciary” and violating Article III.

While discussing how to determine whether Congress had impermissibly intruded into judicial power by allowing an Article I adjunct to adjudicate a private right, Justice Brennan suggested a five-point analysis. This analysis addressed:

1. Whether the adjunct’s jurisdiction extended beyond actions necessary to vindicate congressional intent;
2. Whether the amount of jurisdiction exercised by the adjunct compares to that exercised by Article III judges;

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71 *See, Crowell*, 285 U.S. at 64 (addressing different degrees of deference to be given to the factual records compiled by officers of courts and those compiled by administrative agencies).
72 *Northern Pipeline*, 458 U.S. at 80.
73 *Northern Pipeline*, 458 U.S. at 81-82.
74 *Northern Pipeline*, 458 U.S. at 83-84.
75 “Impermissibly” was Justice Brennan’s choice of words. *See Northern Pipeline*, 458 U.S. 50, 84 n.35 (indicating that the Northern Pipeline decision is not proposing a bright-line analysis of Article I/Article III conflicts).
76 *Northern Pipeline*, 458 U.S. at 84.
3. Whether the adjunct has the other responsibilities and remedies available to him that Article III judges have;

4. How much deference the Article III court has when reviewing the adjunct’s decision; and

5. Whether the adjunct can enter orders or decrees that are binding in the absence of an appeal.\(^{77}\)

Although this analysis was not necessary to the determination of the issues before the Court in *Northern Pipeline*, it influences the balancing tests developed in subsequent decisions.

c. *Thomas and Schor: Applying Northern Pipeline’s Multi-Factor Test to Determine Article III Applicability to Adjunct Adjudications.*

The strict and categorical use of public rights/private rights analysis in Article III matters was already eroding when the *Northern Pipeline* decision was delivered. Two years after the *Northern Pipeline* plurality issued its opinion, the Court issued its decision in *Chevron U.S.A. v. Natural Resources Defense Council*,\(^{78}\) a decision which some suggest started an era of unprecedented judicial deference to administrative rulemaking and adjudication.\(^{79}\) Given *Northern Pipeline’s* plurality status and other trends that were developing in the law at that time, it is not surprising that its limited holding would quickly erode.

Two years after *Chevron* and four years after *Northern Pipeline*, in *Thomas v. Union Carbide Agricultural Products Co.*, the Court upheld a congressional scheme that required private parties to enter into binding arbitration to determine the valuation of certain intellectual


property rights – a private right.\textsuperscript{80} The court rejected a formalistic or abstract Article III inquiry.\textsuperscript{81} The registration of pesticide data that led to the arbitration was an integral part of an agency’s objective to safeguard public health by administering a complex statutory scheme.\textsuperscript{82} The Court held that “a seemingly private right [may be] so closely integrated into a public regulatory scheme as to be a matter appropriate for agency resolution with limited involvement by Article III judiciary.”\textsuperscript{83} In other words, if a private right is closely related to or integrated into a regulatory scheme, it could be removed from initial adjudication by an Article III judge, and, implicitly, from the protections of the Seventh Amendment. This balancing of the application of Article III (as opposed to the strictly categorical approach of \textit{Northern Pipeline}) causes difficulty in determining when the balance is upset and Congress has gone too far. It is also difficult to justify the “blue-pencil” of the Seventh Amendment.

Shortly thereafter, in \textit{Commodity Futures Trading Comm. v. Schor}, while determining whether a congressionally created administrative agency, the Commodity Futures Trading Commission (“CFTC”), could hear a common law counterclaim in an administrative proceeding, the Supreme Court again observed that there were no “formalistic and unbending rules” to determine whether “the adjudication of Article III business in a non-Article III tribunal impermissibly threatens the constitutional integrity of the judicial branch.”\textsuperscript{84} The Court identified two interests that Article III protects: 1) “the role of the independent judiciary within the constitutional scheme of tripartite government,” and 2) the safeguarding of litigants’ “right to

\textsuperscript{80} \textit{Thomas}, 473 U.S. at 576.
\textsuperscript{81} \textit{Thomas}, 473 U.S. at 587.
\textsuperscript{82} \textit{Thomas} 473 U.S. at 589.
\textsuperscript{83} \textit{Thomas}, 473 U.S. at 593-94.
have claims decided before judges who are free from potential domination by other branches of government.

From the outset, Justice O’Connor noted that the 1984 *Chevron* decision required deference to the administrative agency. After determining that the litigant in *Schor* had waived his own interest in Article III resolution by withdrawing a judicial challenge to the administrative proceedings, the Court considered the separation of powers issue. To do so, the Court applied many of the factors developed in *Northern Pipeline* to analyze a judicial adjunct’s jurisdiction to the jurisdiction exercised by an administrative agency in *Schor*. Using this analysis, and noting that the analysis required flexibility, the Court found that allowing the Article I agency to hear common-law counterclaims that were inseparable from the statutory scheme did not offend the separations of powers doctrine. Although *Schor* rejects the proposition that bright-line rules can be effectively applied in Article III inquiries, it impliedly recognizes that although the line is not bright, it might still be found.

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89. *Schor*, 478 U.S. at 856. In *Schor* the claims were inseparable because the claims before the CFTC, one for customer damages incurred by a customer of a commodities trader was inseparable from the trader’s counterclaim for a negative account balance. *Id.*
90. See *Schor*, 478 U.S. at 857 (rejecting bright line rule and holding that scheme in *Schor* provided for administrative jurisdiction over a state law claim that was “a necessary incident” to the legislative scheme).
Applying The Seventh Amendment Right to a Jury Trial to Article I Adjudications.

Seventh Amendment jurisprudence underwent a similar evolution to that of Article III. After remaining relative quiet for many decades, the advent of the New Deal and the administrative state required that courts give the Seventh Amendment and the interests it protects new and deferential consideration. This consideration continued to expand through the late 1980s while the Supreme Court continued to defer to Congress while carefully balancing interests and qualifying decisions to prevent absolute relinquishment of its prerogative to Congress. Now in the post-post Chevron era, the Court may be starting to see the limits to its deference to Congress and its delegation of certain adjudications to Article I bodies.

f. 1937: The Court Defines Three Criteria for Striking a Seventh Amendment Challenge to an Administrative Adjudication of Back Pay in NLRB v. Jones & Laughlin Steel Corp.

The decisions addressed above include little, if any, discussion of the Seventh Amendment guaranty of a jury trial “in cases arising under common law.” This is because, like the jurisprudence that developed around Article III from the New Deal through the late twentieth century, the jurisprudence surrounding the Seventh Amendment struggled to balance the deference to be accorded to executive and legislative regulatory schemes and the Administrative or Article I adjudication they imply against the right of the regulated person to have a jury trial before a tribunal that is not part and parcel of the regulator with which he has a dispute.

In Nat’l Labor Relations Bd., v. Jones & Laughlin Steel Corp., the Court addressed whether an employer’s Seventh Amendment right to a jury trial applied to an administrative
order to pay lost wages to employees. In that case, the Supreme Court addressed a Seventh Amendment challenge to an order of the National Labor Relations Board (“NLRB”) requiring that an employer provide employees who were terminated for labor organizing activities to be reinstated with back pay. Jones & Laughlin claimed that the award of back pay was the equivalent of a money judgment and so implicated the Seventh Amendment right to a jury trial. The Supreme Court’s language rejecting this claim is worth reading because it is so often incompletely quoted:

Thus [the Seventh Amendment] has no application to cases where recovery of money damages is an incident to equitable relief even though damages might have been required in an action at law. [citations omitted] It does not apply when the proceeding is not in the nature of a suit at common law. [citations omitted]

The instant case is not a suit at common law or in the nature of such a suit. The proceeding is a statutory proceeding. Reinstatement of the employee and payment for time lost are requirements imposed for the violation of the statute and are remedies appropriate to its enforcement.

The Court identified three grounds for the inapplicability of the Seventh Amendment: 1) the relief was equitable with monetary penalties being only incidental; 2) this was not an action at common law but an action created by a statute, and; 3) the claims were not analogous to an action at common law because reinstatement and back pay are remedies that are appropriate for the statute’s enforcement.

92 NLRB, 301 U.S. at 22.
93 NLRB, 301 U.S. at 48.
94 NLRB, 301 U.S. at 48-49.
95 Id.
The Court did not hold, as is sometimes suggested, that the Seventh Amendment never applies to statutory actions. It held that the Seventh Amendment did not apply where the monetary penalty was incidental to other equitable relief and appropriate for enforcement of the statute. The *NLRB v. Jones & Laughlin* decision did not address whether the Seventh Amendment applies when the monetary penalty assessed is not wholly incidental to equitable relied and/or has a purpose beyond enforcement of the statute.  

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g. 1974: *In Curtis v. Loether, The Supreme Court Limits Congressional Delegation of Adjudication to Administrative Bodies to Cases Involving Equitable Relief.*

The Court addressed the question of whether a punitive monetary penalty would implicate the Seventh Amendment 37 years later in *Curtis v. Loether.* Curtis was a private action for compensatory and punitive brought under the fair housing provisions of Civil Rights

96 A penalty that goes beyond enforcement of the statute would be one that includes punishment or retribution. Traditionally, administrative agencies were responsible for writing rules, adjudicating their meanings and penalizing violations of those rules sufficiently to induce compliance. Max Minzer, *Why Agencies Punish*, 53 WM.&MARY L.REV. 853, 856 (2012). Agencies did not involve themselves in retributive adjudications, i.e., punishment imposed for the sake of punishment itself; that was left for law enforcement authorities. *Id.* Courts avoided involvement in the adjudications of disputes arising out of administrative determinations because doing so would result in the courts getting involved in political determinations that could be overruled by Congress or the Executive and cause dilution of the courts’ authority. Thomas W. Merrill, *Article III, Agency Adjudication, and the Origins of the Appellate Review Model of Administrative Law*, 111 COLUM. L. REV. 939, 988-91 (2011). Therefore, an award of back pay or a limited liquidated penalty would be appropriate for enforcement of a statute. However, as penalties become less directly tied to equitable relief or increase sufficiently to seem punitive without becoming criminal, they could become something more than a means of enforcing the statute and so implicate the Seventh Amendment.

Act of 1968.\(^98\) The defendant’s jury trial demand was stricken and after a trial at which the plaintiff was awarded no compensatory but $250 in punitive damages, the defendant appealed raising the jury trial issue.\(^99\) The Court rejected the plaintiff/appellee’s argument that \textit{NLRB v. Jones & Laughlin Steel} held that the Seventh Amendment did not apply to statutory actions, stating that:

> The Seventh Amendment does apply to actions enforcing statutory rights, and requires a jury trial upon demand, if the statute creates legal rights and remedies, enforceable in an action for damages in the ordinary courts of law.\(^100\)

\textit{NLRB}’s holding was limited to matters in which a jury trial would be “incompatible with the concept of administrative adjudication.”\(^101\) The Court did not say what circumstances would make a jury trial incompatible with administrative adjudication. However, the Court continued to hold that if a remedy flowing from a statutory rights sounds in equity, Congress can “entrust” its adjudication to “administrative or specialized courts.”\(^102\) If Congress provided for enforcement in a district of a right or remedy that sounded in law, the Seventh Amendment would attach to that adjudication.\(^103\)

\(^98\) \textit{Curtis}, 415 U.S. at 190.
\(^99\) \textit{Curtis}, 415 U.S. at 191.
\(^100\) \textit{Curtis}, 415 U.S. at 193-94.
\(^101\) \textit{Curtis}, 415 U.S. at 195.
\(^102\) \textit{Id.} (citing, \textit{Katchen v. Landy}, 382 U.S. 323 (1966)(denying Seventh Amendment challenge to Bankruptcy Court’s jurisdiction over trustee’s action to compel surrender of voidable preference payment because Bankruptcy Court was traditionally one of equity that was necessary for goals of Bankruptcy Code); \textit{Guthrie Nat’l. Bank Guthrie}, 173 U.S. 528 (1899)(Congress’ creation of special territorial tribunals for adjudication of claims regarding indebtedness incurred by territorial governments did not offend the Seventh Amendment).
\(^103\) \textit{Id.}
The Court did not address what should occur if Congress assigned the adjudication of a legal claim to an administrative court. However, it suggests that Congress may not have ability to assign legal claims to which a jury trial rights attaches to non-Article III tribunals. Moreover, this decision suggests that when the penalty is punitive, like the damages asserted in Curtis, it is the “traditional form of relief offered in the courts of law” and so subject to the Seventh Amendment.104

h. 1977: Atlas Roofing and the Merger of Article III and Seventh Amendment Analysis.

With its 1977 decision in Atlas Roofing Co., Inc. v. Occupational Safety and Health Review Comm., the Supreme Court disposed of the historical “suits at common law” analysis underlying Seventh Amendment analysis and applied Article III’s public right/private right analysis to both Article III and the Seventh Amendment questions.105 That case involved a Seventh Amendment challenge to two workplace hazard abatement orders and civil penalties of $5,000 for one appellant and $600 for another imposed by OSHA. Showing extreme deference to Congress, the Court brought the jury question “under the rubric of the public rights doctrine,” applied the public rights analysis developed under Article III, and held that if the right in question was a public right susceptible of administrative adjudication, then the Seventh Amendment need not come into play.106 The Court further clarified that “[t]his is the case even if the Seventh Amendment would have required a jury where the adjudication of those rights is assigned to a federal court of law instead of an administrative agency.” 107 In other words, the

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104 Curtis, 415 U.S. at 195-96.
106 Atlas Roofing, 430 U.S. 442 at 455.
107 Id.
broadest reading of *Atlas Roofing* suggests that Congress can legislate away the Article III and Seventh Amendment protections at will.

However, in the final footnote to *Atlas Roofing*, the Court suggested that Congress’ ability to delegate rights and remedies away from Article III courts and Seventh Amendment jury trials was not unlimited. The Court wrote:

> Petitioners claim that permitting Congress to control the jury-right question by picking the forum is to delegate to it, rather than this Court, the final power to decide the Seventh Amendment issues. The claim in incorrect. The Seventh Amendment prevents Congress from depriving a litigant of a jury trial in a “legal” action before a tribunal customarily utilizing a jury as its fact finding arm, [citation omitted], and this Court has the final decision on the question whether a jury is required.\(^\text{108}\)

The Court made it clear that Congress’ ability to delegate questions away from Article III courts with Seventh Amendment protections was not unlimited and would be decided by courts. Given the minimal penalties at issue in *Atlas Roofing*, the question that was implied since *Nat’l Labor Relations Bd., v. Jones & Laughlin Steel Corp.*, whether the Seventh Amendment applied to question of punitive yet not criminal monetary penalties, was not addressed.

\textit{i. 1987: In *Tull*, the Supreme Court Differentiates Between Different Types of Penalties When Applying the Seventh Amendment.}

Ten years later, in *Tull v. United States*\(^\text{109}\), the Court recognized the limitations of its holding in *Atlas Roofing*. The Court stated that:

> In *Atlas Roofing Co. v. Occupational Safety and Health Review Comm’n.*, [citation omitted], we explicitly declined to decide whether the dictum of *Hepner* and *Regan*[that the Seventh Amendment jury trial guarantee

\(^{108}\) *Atlas Roofing*, 430 U.S. 442 at 455.

applies to civil actions to attempt a civil penalty] “correctly divines the intent of the Seventh Amendment.\textsuperscript{110}

The \textit{Tull} Court recognized that there are more than one type of penalty, that \textit{Atlas Roofing} addressed only one type and that different types of penalties come with different constitutional protections. The Court resolved the question of what penalties came with what protections by looking at “both the nature of the action and of the remedy sought …”\textsuperscript{111} While considering the nature of the action, the Court observed that, at common law, actions for civil penalties were analogous to common law action for a debt.\textsuperscript{112} The Court continued to hold that the nature of the penalties, a claim of $22 Million for violations of the Clean Water Act and a judgment of $325,000 were punitive in nature.\textsuperscript{113} “Remedies intended to punish culpable individuals, as opposed to those intended simply to extract compensation or restore the status quo, were issued by courts of law, not equity.”\textsuperscript{114} The Court found that because there was just a daily fine of $10,000, without any calculation of equitable concerns, \textit{e.g.}, ill-gotten gains, the remedy was a punitive one that required a jury trial for the liability phase of the trial.\textsuperscript{115} \textit{Tull} holds that Seventh Amendment protections do not attach to non-punitive penalties like those assessed in \textit{Atlas Roofing}. \textit{Tull} also shows that \textit{Atlas Roofing} cannot be read so broadly as to take away the Seventh Amendment jury trial right away from one against whom a punitive penalty is assessed.

\begin{enumerate}
\item[\textsuperscript{110}] \textit{Tull}, 481 U.S. 416-17.
\item[\textsuperscript{111}] \textit{Tull}, 481 U.S. at 417.
\item[\textsuperscript{112}] \textit{Tull}, 481 U.S. at 418. Implicitly, then, the fines in \textit{Atlas Roofing} were something other than civil penalties.
\item[\textsuperscript{113}] \textit{Tull}, 481 U.S. at 420, 422.
\item[\textsuperscript{114}] \textit{Tull}, 418 U.S. at 422.
\item[\textsuperscript{115}] \textit{Id.}
\end{enumerate}
j. 1989: In Granfinanciera, the Supreme Court Strikes Down a Congressional Delegation of a Common Law Claim to an Article I Court on Seventh Amendment Grounds.

Twelve years later, the Supreme Court again considered which types of claims Congress could take away from Article III jury trials. In Granfinanciera, N.A. v. Nordberg, the United States Trustee, a government employee, brought fraudulent conveyance claims against a creditor in a United States Bankruptcy Court. The creditor challenged the Bankruptcy Court’s jurisdiction because fraudulent conveyance claims arose at common law and were subject to the Seventh Amendment’s right to a jury trial. Justice Brennan, writing for a majority, held that claims for fraudulent conveyances, even when brought by a United States Trustee as part of bankruptcy proceedings, were claims for money at common law that involved “the liability of one individual to another under the law as defined” and were subject to the Seventh Amendment right to a jury trial. The majority recognized that Congress could not:

… strip parties contesting matters of private right of their constitutional right to a trial by jury. As we recognized in Atlas Roofing, to hold otherwise would be to permit Congress to eviscerate the Seventh Amendment’s guarantee by assigning to administrative agencies or courts of equity all causes of action not grounded in state law, whether they originate in a newly fashioned regulatory scheme or possess a long-line of common-law forebears.

Thus, even if a regulatory scheme substitutes the federal government as a plaintiff in a matter that previously was a matter solely between private parties, if the common law precedent included the right to a jury trial, the jury trial right remains. With Granfinanciera, the Court

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117 Granfinanciera, 492 U.S. at 41.
118 Granfinanciera, 492 U.S. at 51.
119 Granfinanciera, 492 U.S. at 52.
120 Id.
finally struck down Congressional action that offended Article III and the Seventh Amendment, and provided a formula for analyzing these challenges: if the claim is legal and a public right, there is no jury right; but if it is legal and a private right, there is.\textsuperscript{121} Furthermore, even though Congress can legislate broadly, it cannot legislate so broadly as to “eviscerate the Seventh Amendment’s guarantee by assigning to administrative agencies or courts of equity all causes of action not grounded in state law, whether they originate in a newly fashioned regulatory scheme or possess a long-line of common-law forebears.”\textsuperscript{122}

3. Reconciling the Article III and Seventh Amendment Cases.

The decision in \textit{Granfinanciera} is consistent with dicta in \textit{Schor}. In \textit{Schor}, although Justice O’Connor deferred to Congress’ authority to create an Article I tribunal that adjudicated private rights because the rights at issue were inextricably tied to the regulatory scheme, she conceded that judicial review of congressional assumption of the adjudication of private rights must be “searching.”\textsuperscript{123} It is also consistent with Justice Blackmun’s dissent in \textit{Granfinanciera} in which Justice O’Connor joined. Justice Blackmun wrote:

\begin{quote}
… it must be acknowledged that Congress has legislated treacherously close to the constitutional line by denying a jury trial in a fraudulent conveyance action in which the defendants has no claim against the estate. Nonetheless, given the significant federal interests involved, and the importance of permitting Congress at long last to fashion a modern bankruptcy system which places the basic rudiments of the bankruptcy
\end{quote}

\textsuperscript{121} \textit{Granfinanciera}, 492 U.S. at 53.

\textsuperscript{122} \textit{Granfinanciera}, 492 U.S. at 52.

\textsuperscript{123} \textit{Schor}, 478 U.S. at 843 (searching review of Congressional action on private rights); 478 U.S. at 854 (actions at common-law would remain subject to jury trial if separable from comprehensive legislative scheme).
process in the hands of an expert equitable tribunal, I cannot say that Congress has crossed the constitutional line on the facts of this case. 124

Therefore, when Atlas, Northern Pipeline, Schor and Granfinanciera are read as a whole, they show that the question of addressing an Article I/Article III conflict is whether, when applying a deferential review of Congressional action, Congress “crossed a line” and offended Article III and/or the Seventh Amendment when it delegated the adjudication of private rights that were not inextricably linked with a regulatory goal to an administrative tribunal.

Although the “bright line” analysis of Northern Pipeline may no longer be applicable, it is also clear that Atlas Roofing’s absolute deference to Congressional stripping of Article III and Seventh Amendment protection is also no longer applicable. The questions are: where is the line, and how do we know when Congress has crossed it.

The more immediate question for purposes of this Article is whether, during the course of Congress’ steady expansion of the SEC’s remedies from 1984 through 2010 (particularly when it allowed the SEC to use its administrative proceedings to collect damages for private investors from both registered and non-registered individuals), Congress crossed the Article III/Seventh Amendment line discussed in Northern Pipeline and Granfinanciera. A test for determining whether that line has been crossed is discussed below.


In 2011, with its decision in Stern v. Marshall, the Supreme Court addressed the question of whether a bankruptcy court created by Congress pursuant to Article I and empowered to adjudicate a common law counterclaim violated the protections of Article III and the Seventh Amendment.

124 Granfinanciera, 492 U.S. at 94 (Blackmun, in dissent).
Amendment. 125 *Stern*, like *Northern Pipeline* and *Granfinanciera* before it, was a challenge to provisions of the United States Bankruptcy Code. Specifically, it was a challenge to 11 U.S. C. § 157(b)(2), that allowed “all counterclaims by the [bankrupt] estate against persons filing claims against the estate” to be tried by the Bankruptcy Court as “core proceedings.” 126 Relying on *Northern Pipeline*, *Granfinanciera* and *Schor* 127, the Supreme Court held that although the statute permitted such a broad definition of the core proceedings over which the Article I Bankruptcy Court could have jurisdiction, Article III did not. 128

The Court set the following three prong test for determining whether Congress has encroached on Article III:

1. Is the action based on a statutory right that:
   a) is closely entwined with a federal regulatory program, and
   b) belongs to or exists against the United States; or is the action;

2. “Quintessentially a suit at common law that resembles a state law claim brought to recover damages,” and

3. Is the subject matter of the claim “a particularized area of the law that requires an expert and inexpensive method for dealing with a class of questions of fact which are particularly suited to examination and determination by an administrative agency specifically assigned to that task.”129

The Court considered whether the right at issue was: 1) purely a creation of statute – a public right, or 2) one that arises at common law to which a right to a Seventh Amendment jury trial


126 *Stern*, 131 S. Ct. at 2601.

127 *Stern*, 131 S.Ct. at 2604-05.

128 *Stern*, 131 S.Ct. at 2608.

129 *Stern*, 131 S.Ct. at 2613-14.
might attach, but is, nevertheless 3) one whose adjudication is so necessary to a comprehensive legislative regulatory scheme that it must be converted to a public right with limited Article III review and no Seventh Amendment protections. Mere inclusion of an adjudicatory body or method within a statute did not necessarily constitute a “federal regulatory scheme” that would allow encroachment into matters preserved for adjudication within Article III; to do so would allow Congress to transform a private right into a public one at will.  

The Court applied this test to the tortious interference claim in *Stern* and found that, although the claim might be based on a statutory right provided by the Bankruptcy Code, it was not so closely entwined with Congress’ goal in enacting the Bankruptcy Code’s goal, *i.e.*, the goal of providing a hierarchical ordered claims process for distributing pro rata shares of the bankruptcy *res* for the benefit of the creditors. As such, the claim was “one under state common law between two private parties.” Furthermore, these common law claims did not pose a situation in which “Congress devised an expert and inexpensive method for dealing with a class of questions of fact which are particularly suited to examination and determination by an administrative agency.” Having made this determination, the Supreme Court affirmed the Circuit Court’s order vacating the Bankruptcy Court’s determination of the counterclaim.

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130 *Stern*, 131 S.Ct. at 2615.
131 *Stern*, 131 S.Ct. at 2614-15.
132 *Stern*, 131 S.Ct. at 2614-15
133 *Id.*
134 *Stern*, 131 S.Ct. at 2615.
D. Does Stern v. Marshall Apply to the SEC’s Administrative Proceedings?

The question, then, is whether and how the Stern decision applies to the SEC’s ability to adjudicate claims for monetary penalties against unregulated persons through administrative proceedings. The Stern decision is specifically limited to Article I courts:

We recognize that there may be instances in which the distinction between public and private rights – at least as framed by some of our recent cases-fails to provide concrete guidance as to whether, for example, a particular agency can adjudicate legal issues under a substantive regulatory scheme. Given the extent to which this case is so markedly distinct from the agency cases discussing the public rights exception in the context of such a regime, however, we do not in this opinion express any view on how the doctrine might apply in that different context.135

The issue of how this analysis now applies to agency adjudications was not before the Court in Stern.

1. Applying the Stern Test to Administrative Agency Adjudications Is Consistent with Precedent.

However, the “recent cases” referred to in Stern are those described above: Crowell v. Benson; Northern Pipeline Construction Co. v. Marathon Pipe Line Co.; Thomas v. Union Carbide Agricultural Products, Co.; Commodity Futures Trading Commission v. Schor; and Granfinanciera, S.A. v. Nordberg.136 Crowell was a case that addressed whether an administrative agency’s adjudication of a private right unnecessarily encroached on Article III.137

In Northern Pipeline, a case like Stern that addressed the ability of an Article I United States Bankruptcy Court to determine a matter of private right, the Court cited and applied Crowell to emphasize that it is the controversy that is removed from the Article III court, not the court or

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135 Stern, 131 S.Ct. at 2615.
136 Stern, 131 S.Ct. at 2609, 2612-14.
137 Crowell, 285 U.S. at 48-49.
administrative agency to which it is removed, that matters for purposes of separations of powers analysis. In Schor, an administrative agency case, the Court made no distinctions between administrative agencies and judicial courts when discussing the removal of issues from Article III cognizance. Thomas, an agency case, also relies on Northern Pipeline while making no distinction between courts and agencies. Similarly, in Granfinanciera, another bankruptcy court case, albeit one in which a Seventh Amendment right was asserted, the Court considered the relationship of the adjunct to the right at issue, the availability of review by an Article III Court, and the applicability of the Seventh Amendment. The Court did not distinguish between agencies and courts as the types of “administrative agencies or other tribunals not involving juries” that Congress can create.

All of these cases recognize that the dispositive issue is not whether Congress characterizes the tribunals it creates as a court or an agency; it is the nature of the controversy that Congress delegates to it and how that tribunal functions in relation to Article III and the Seventh Amendment. Therefore, these precedents give no reason to distinguish between Article I courts and administrative agencies when determining whether Congress unduly encroached on

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138 Northern Pipeline, 458 U.S. at 83. Moreover, in his dissent in Schor, Justice Brennan did not distinguish between administrative agencies and Article I court as adjudicators; he cautioned against the use of any “non-Article III tribunals equipped to handle the business of the Article III courts. Schor, 478 U.S. at 866.

139 Schor, 478 U.S. at 853-54.

140 Thomas, 473 U.S. at 584.

141 Granfinanciera, 492 U.S. at 55

142 Granfinanciera, 492 U.S. at 55 n.10.
Article III powers and Seventh Amendment protections. *Stern* can be applied to agency adjudications including the SEC’s administrative proceedings.\(^{143}\)

2. **Congressional Action, As Opposed to Agency Action, Is Not Subject to *Chevron* Deference In A Declaratory Judgment Action.**

In *Schor*, Justice O’Connor suggested that the Supreme Court’s decision in *Chevron U.S.A. v. Natural Resources Defense Council* required some degree of deference to the CFTC’s adjudication.\(^{144}\) *Chevron* was a challenge to the Environmental Protection Agency’s application of its own definition of a statutory term, “stationary source of pollution,” in the absence of a statutory definition of that term.\(^{145}\) The issue in *Chevron* was the amount of deference to be accorded to an administrative agency’s actions regarding its interpretation of the statutes it enforced in the absence of congressional guidance.\(^{146}\) *Chevron* addressed whether an administrative agency acted appropriately within the grant of power made to it by Congress; it did not address whether Congress’ grant of that power was appropriate or a violation of

\(^{143}\) It is true that, in *Stern*, the majority suggested that an adjunct’s court’s ability to enter orders and judgments might distinguish it from the acts of an agency. *Stern*, 131 S.Ct. at 2619. However, the SEC’s ALJ’s are empowered to undertake numerous judicial acts. The Administrative Procedures Act permits an ALJ to:”(1) administer oaths and affirmations;(2) issue subpoenas authorized by law;(3) rule on offers of proof and receive relevant evidence;… (10) make or recommend decisions in accordance with section 557 of this title; and(11) take other action authorized by agency rule consistent with this subchapter.”5 U.S.C.§556(c). Furthermore, the Court noted that the bankruptcy courts in *Stern* and *Northern Pipeline* both attributes satisfied part of the analysis for determining encroachment on Article III because their judgments became final if not appealed. *Stern*, 131 S.Ct. at 2619. Similarly, the determinations of both the SEC ALJ, and the Commission itself, become final if not appealed. SEC ROP 360(d).


\(^{145}\) *Chevron U.S.A.*, 467 U.S. at 841.

\(^{146}\) *Chevron*, 467 U.S. at 842-44.
separation of powers. When a Court must address whether Congress, not the administrative agency, acted appropriately, no Chevron deference is required or even appropriate.\textsuperscript{147} Indeed, when the Supreme Court addressed the separation of powers issues in Free Enterprise Fund, there was no discussion of Chevron in the majority opinion.\textsuperscript{148}

Moreover, Schor was not, as Free Enterprise Fund was, a facial challenge to pending administrative proceedings. Schor was an appeal of actions and decisions that the agency had already made.\textsuperscript{149} Therefore, Chevron was applicable to Schor to the extent that Schor included a challenge to agency’s decisions and actions. Free Enterprise Fund was not a challenge to the agency’s actions so much as a challenge to the Congress’ delegation of the authority to act.\textsuperscript{150}

\textbf{E. Applying Stern to Administrative Adjudications}

The final step is to determine how Stern and the authorities on which it is based would apply to the SEC’s administrative proceedings against unregulated persons. To do this analysis, each prong of the test proposed by Stern will be treated as a separate sub-heading. The analysis

\begin{itemize}
  \item \textsuperscript{147}Peter L. Strauss, Deference Is Too Confusing – Let’s Call Them “Chevron Space” And “Skidmore Weight” 112 COLUM.L.REV. 1143, 1145 (2012).
  \item \textsuperscript{148}See Free Enterprise Fund, 561 U.S 477 (2010)(generally).
  \item \textsuperscript{149}Schor, 478 U.S. at 836.
  \item \textsuperscript{150}This is not to say that Congressional action is not entitled to any deference. As noted in Stern, courts must “construe federal statutes so as to avoid serious doubt of their constitutionality. Stern, 131 S.Ct. at 2605. However, as Stern also shows, this deference is not unlimited. A court cannot ignore the language of or rewrite a statute “to avoid constitutional adjudication.” Stern, 131 S.Ct. at 2605. The Court continued to suggest that the deferential review of Article I action seen in Schor and Thomas may no longer be applied. “A statute may no more lawfully chip away at the authority of the Judicial Branch than it may abolish it entirely.” Stern, 131 S.Ct. at 2620. “Slight encroachments create new boundaries from which legions of power can seek new territory to capture.” Id.
\end{itemize}
of any single aspect of such application of *Stern* is highly dependent on the facts surrounding each defendant and the relief sought by the SEC.

1. **Is the Action a Statutory Right That Is Closely Entwined With a Federal Regulatory Program and Belongs or Exists Against the United States?**

   This first aspect of the test represents the Article III interest: is this a congressionally-created public right or a private right necessarily included in a comprehensive statutory scheme. This prong of the test has two subparts: 1) is the action a statutory right entwined with a federal program, and; 2) does it belong to or exist against the United States.\(^{151}\)

   Equitable claims against regulated persons would be statutory rights that are closely entwined with a federal regulatory program; this is, after all, the original jurisdiction of the SEC.\(^{152}\) Similarly, the pursuit of monetary penalties in the form of disgorgement against those who must register with the SEC comprise equitable relief and are within the original statutory mandate of the SEC.\(^{153}\)

   However, as the focus of administrative proceedings moves away from equitable relief against regulated persons, the question of whether the action is a statutory right that is necessarily entwined with a federal regulatory program becomes less clear. The Sarbanes-Oxley Act of 2002 permits the SEC to pursue penalties not for pure enforcement purposes but to collect funds for defrauded investors.\(^{154}\) As the Court recognized in *Northern Pipeline* and *Granfinanciera*, even if the federal government is the actual party, if the purpose of the action is

\(^{151}\) *Stern*, 131 S.Ct. at 2613.

\(^{152}\) Atkins, Bondi, n.1 *supra* at 383-84; Black, n.2 *supra* at 322.

\(^{153}\) See *Securities & Exchange Comm. v. Rind*, 991 F.2d 1486, 1491 (9th Cir. 1993)(disgorgement is an equitable remedy included within the SEC’s mandate to enforce the securities laws).

\(^{154}\) Sarbanes-Oxley Act §308; Spehr, n.10 *supra* at 590.
recovery for a private party, the action is one for the private right. Further, as *Tull* made clear, the recovery of statutory penalties is often construed as an action for a debt and is considered a common law claim with the protections accorded such claims.\(^{155}\) Therefore, and particularly if the action is based on shareholders losses and recoveries, an action for shareholder recovery or monetary penalties is not a public right.

2. **Or, Is the Action “Quintessentially A Suit at Common Law That Resembles a State Law Claim to Recover Damages?”**

The language of this element of the *Stern* test follows the language of the Seventh Amendment. The test for whether an action “is quintessentially an action at common law” is found in *Tull*.\(^{156}\) As discussed above, in *Tull*, the Court considered whether a defendant had a Seventh Amendment right to a jury trial in an action for penalties assessed under the Clean Water Act. Where the statute was silent as to whether there was a jury trial right, the Court held that actions for penalties under a statute were analogous to actions for debt in the English common law courts and, as such, guaranteed a right to a jury trial.\(^{157}\) At least one court has relied upon the holding in *Tull* to argue that a constitutional right to a jury trial, not a mere statutory right to one, attaches to an action brought by the SEC under Section 10(b) of the Securities Exchange Act.\(^{158}\) To the extent the claim is for Fair Funds recoveries, it is difficult to tell how these recoveries for the benefit of shareholders is anything other than a matter of private right.


\(^{156}\) Tull v. United States, 481 U.S. 412 (1987). The test described in *Tull* has been applied to securities actions. See, Rind, 991 F.2d at 1493 (applying *Tull* to SEC disgorgement proceedings to determine whether a Seventh Amendment jury right attaches).

\(^{157}\) Tull, 481 U.S. at 419-20.

like those at issue in *Northern Pipeline* and *Granfinanciera*, even if a government agency, like that in *Granfinanciera*, is standing in the shoes of the private party. Even if the recovery is not used for Fair Funds recovery, *Tull* and the common law underlying hold that the government is acting as a private party when recovering these penalties.

Application of the *Tull* test to an administrative proceeding brought by the SEC would, again, depend upon the facts of the given case. *Tull* would not provide any grounds to challenge an action for disgorgement or any other form of equitable relief brought against a directly regulated person. Similarly, a claim for disgorgement, if determined to be purely equitable, would not implicate a Seventh Amendment right to a jury trial for an unregulated person. However, a claim for either tiered penalties or Fair Funds recovery against an unregulated person would implicate a Seventh Amendment right to a jury trial. Therefore, because claims for statutory penalties and/or shareholder recovery are analogous to an action at common law, this second prong of the test stated in *Stern* may be satisfied by a facial challenge to the SEC’s administrative jurisdiction.

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159 *Solow*, 554 F.Supp.2d at 1367.

3. **Is the Subject Matter Of The Claim a Particularized Area of Law That Requires An Expert and Inexpensive Method for Dealing With Questions of Fact That Are Particularly Suited to An Administrative Agency?**

This final prong seems the most difficult to challenge. One Court has held that the mere fact that Congress creates an administrative agency to administer a statutory scheme, rather than a court, indicates congressional intention to create a public right that is not subject to the Seventh Amendment.\(^{161}\) Consideration of the history of the SEC’s enforcement efforts and, in particular, the history of allowing private rights of action for enforcing the securities statutes, suggests that Congress never intended for the enforcement of these statutes to be a wholly public right to be solely administered by the SEC.

When Congress created the SEC in 1934, many of the remedies and actions available to it now were not available. As discussed above, between 1934 and the late 1980s, the SEC was limited to obtaining equitable relief in the United States District Courts against directly regulated persons: bankers, underwriters and broker-dealers.\(^{162}\) The ability to recover disgorgement and monetary penalties against regulated and unregulated persons came during the late 1980s and the mid-1990s.\(^{163}\) The SEC did not pursue recovery of penalties for repayment of investors until

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\(^{161}\) See Securities Investor Protection Corp. v. Bernard L. Madoff Investment Securities, LLC, 490 B.R. 46, 55 (S.D.N.Y. 2013)(“whenever the Supreme Court has held that a federal regulatory scheme creates a public right, a regulatory agency has administered that scheme”) aff’d., 740 F.3d 81 (2d Cir. 2014).

\(^{162}\) Black, n.2 supra at 322.

\(^{163}\) See Insider Trader Sanctions Act of 1984 § 2 (codified as amended throughout 15 U.S.C.) (empowering SEC to pursue civil monetary penalties of up to three times the profit realized or the loss avoided as a result of insider trading in United States District Court proceedings); Insider Trading and Securities Fraud Act of 1988§ 3 (codified as amended throughout 15 U.S.C.) (allowing SEC to recover monetary penalties, through a jury trial in the United States District Courts, from controlling persons of those who trade on material non-public information in violation of the law); Securities Enforcement Remedies and Penny
Administrative recoveries of these penalties from unregulated persons were not permitted until 2010. Thus, the SEC, as formed by Congress in 1934, had a much different mission and much more limited remedies available to it than the one with which we are presented today. The collection of monetary penalties, except as necessary for disgorgement, was not only not part of the agency’s mission, but antithetical to it. The formation of the SEC in 1934 is not dispositive of congressional intention today regarding whether shareholder recovery is so intertwined with the regulation of the securities markets that it cannot be severed from other regulatory functions and so must be considered a public right.

Moreover, private rights of actions for damages have always been an important part of securities law. The Securities Act of 1933 expressly provided a private right of action against signers of registration statements that included material misrepresentations or omission. The Securities Exchange Act of 1934 also included a private right of action allowing investors to sue

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164 See, Sarbanes-Oxley Act of 2002, § 308. See Section I above. Even after the SEC, with the passage of Sarbanes-Oxley, took up the pursuit of damages in some cases, the private rights of action remain. So although the Congress formed the SEC in 1934 to enforce some claims and pursue some types of relief, it has never been the exclusive pursuer of claims and damages.

165 See Section I.C, above.

166 See Atkins, Bondi, n.1 supra. at 384.

for manipulation or deception, insider trader profits, and false or misleading statements.\textsuperscript{168} Since at least 1946, only thirteen years after the formation of the SEC, the courts have recognized a private right of action under Rule 10(b) of the Securities Exchange Act of 1934 for violations of the use or employment of “any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, or any securities-based swap agreement.”\textsuperscript{169}

Given the broad and long-standing use of Section 10(b) and other private rights of action in private securities litigation, one would be hard-pressed to argue that Congress intended the enforcement of the securities laws to be solely the province of the federal government and its agencies. Even the Dodd-Frank amendments to the securities laws contemplated private actions by ordering a General Accountability Office study on the viability of private actions under those amendments for aiding and abetting.\textsuperscript{170} Thus, the enforcement of and assertion of rights under at least certain sections of the securities laws has always been a matter of some private action. The question is whether an action for monetary penalties is included within one of those private rights actions and requires Article III adjudication and/or a Seventh Amendment jury trial.

\textit{Granfinanciera} provides guidance. In that case, Justice Brennan looked to the nature and purpose of the action and its role in the overall statutory scheme to determine whether Congress


had legislated over an Article III adjudication and a Seventh Amendment right to a jury trial.\textsuperscript{171}

He found that those actions to reverse fraudulent conveyances:

\[
\ldots \text{constitute no part of the proceedings in bankruptcy but concern}
\]

controversies arising out of it – are quintessentially suits at common law

that more resemble state law contract claims brought by a bankrupt
corporation to augment the bankruptcy estate than they do creditors’
hierarchically ordered claims to a \textit{pro rata} share of the bankruptcy res.

They therefore appear matters of private rather than public right.\textsuperscript{172}

One must ask the same action when considering SEC administrative actions: whether there is a

crucial part of the regulatory scheme such as the pursuit of disgorgement and other equitable

remedies against directly regulated persons, or an act to recover penalties (under \textit{Tull}, a common

law action) or some other action to recover funds for third parties. If the action is either of the

latter two, this final prong of the \textit{Stern} is satisfied, the statute allowing the administrative action

would be an impermissible encroachment on Article III and the Seventh Amendment and a facial

challenge to an SEC administrative action could be asserted.

\section*{IV. Conclusion}

Whenever Congress creates a new regulatory scheme or expands an existing one, that

scheme must include penalties. Without them, the scheme would be unenforceable. History

shows us that monetary penalties are among the most effective. The continuing question is

whether the levying and pursuit of these monetary penalties should be adjudicated in the first

instance by the regulating agency or by an Article III court and a jury. Since the 1930s, courts

have tried to balance their obligation to be deferential to Congressional determinations about the

need for efficient administrative enforcement of new laws against the necessity to protect the

courts and the general population from agencies that act as policeman, judge, jury and

\textsuperscript{171}\textit{Granfinanciera}, 492 U.S. at 54-55.

\textsuperscript{172}\textit{Granfinanciera}, 492 U.S. at 56. [citations omitted]
executioner. In *Stern v. Marshall*, the Supreme Court presented an evolved and comprehensive test for determining whether Congress overreached when it included certain claims within the jurisdiction of an Article I tribunal. There is no reason not to apply this test to the question of whether the SEC can pursue monetary penalties against unregulated persons, such as officers and directors of regulated persons, through administrative proceedings. Application of the *Stern* test through a facial challenge to such a proceeding may be successful.