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Second Circuit Limits Judicial Review of SEC Settlements

When a district court judge in the Southern District of New York refused to approve a carefully negotiated consent settlement between the U.S. Securities and Exchange Commission ("SEC") and Citigroup Global Markets, Inc. ("Citigroup") in November 2011, the decision sent shockwaves through corporate America. Numerous commentators expressed concern that such judicial second-guessing would undermine the certainty companies appropriately seek through negotiated settlements (see our prior memos here and here). Echoing those concerns, the Second Circuit Court of Appeals stayed the district court order in March 2012 (link), finding that the SEC had demonstrated a "strong likelihood of success" on the merits of its appeal from the district court's order refusing to approve the consent decree. In a unanimous and strongly worded opinion issued yesterday (link), the Second Circuit hewed to that finding and reversed the district court. In so doing, the Court strongly reaffirmed the bedrock principle that the parties to a controversy are best positioned to evaluate the competing considerations that inform the decision to settle. As the Court noted, "[c]onsent decrees provide parties with a means to manage risk" and such "assessments are uniquely for the litigants to make."

The Court of Appeals also rebuked the district court for failing to accord the SEC the "significant deference" its policy judgments are owed, including with respect to whether, when and how to resolve enforcement proceedings. Holding that the district court had committed "legal error" by interposing its own views on whether the proposed consent decree had served the public interest, the Second Circuit observed that "[t]he job of determining whether the proposed SEC consent decree best serves the public interest rests squarely with the SEC." The Second Circuit thus reminded the lower courts, "[w]hat the district court may not do is find the public interest disserved based on its disagreement with the SEC's decisions on discretionary matters of policy, such as deciding to settle without requiring an admission of liability."

The Court of Appeals's opinion also importantly clarifies that the appropriate standard of review is far narrower than that employed by the district court in the *Citigroup* case. In reviewing proposed consent decrees, "the district court must determine whether the proposed consent decree is fair, reasonable" and, if an injunction is being sought, that "the public interest [will] not be disserved." The Court underscored the import of that limited scope of review: "[a]bsent a substantial basis in the record for concluding that the proposed consent decree does not meet these requirements, the district court is required to enter the order." The opinion thus makes it clear that reviewing courts are not permitted to substitute their own views of the types of charges the SEC may choose to resolve in a settlement or the levels of financial payments to be made pursuant to a negotiated consent decree, and may not insist upon admissions of facts as a condition of settlement.

The Second Circuit's decision therefore reaffirms that the SEC's longstanding policy of entering into "no admit/no-deny" settlements is entitled to substantial deference and is entirely proper. Moreover, the opinion signals that when carefully negotiated resolutions are presented to reviewing courts and are supported by a reasonable basis, they should be and will be approved.

Consistent with its own principle of according substantial deference to SEC enforcement policy judgments, the Second Circuit's opinion does not prevent the SEC itself from seeking an admission of liability as a term of settlement in particular cases. In fact, SEC Director of Enforcement Andrew Ceresney has already announced publicly that, while the SEC is pleased with the Second Circuit's decision, the agency "will continue to seek admissions in appropriate cases." It is worth remembering, however, that those types of settlements have been relatively rare. It is likely, especially in light of the Second Circuit's *Citigroup* opinion, that the vast majority of SEC settlements will continue to be done on a "no admit/no deny" basis.

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