UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

RAJAT K. GUPTA,	:	
	:	11-cv-01900 (JSR)
Plaintiff,	:	
v.	:	
SECURITIES AND EXCHANGE COMMISSION,	:	
Defendant.	:	

MEMORANDUM OF LAW IN SUPPORT OF MOTION TO DISMISS COMPLAINT

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This Court should dismiss Gupta's complaint for lack of subject matter jurisdiction under Fed. R. Civ. P. 12(b)(1) and failure to state a claim under Fed. R. Civ. P. 12(b)(6).

INTRODUCTION

The Securities and Exchange Commission's Division of Enforcement ("Enforcement") is prosecuting an administrative proceeding against Rajat K. Gupta in which it alleges that he violated antifraud provisions of the federal securities laws by providing material inside information to Raj Rajaratnam who then traded based on that information. The order instituting the administrative proceeding ("OIP") identifies several remedies that could be applied if Gupta is found to have committed the alleged violations, including a cease-and-desist order, an officer-and-director bar, disgorgement, and civil penalties. The OIP cites three separate and independent statutory bases upon which the SEC is authorized to impose penalties in the event that Gupta were found to have violated the federal securities laws, including long-standing provisions that authorize such penalties against persons who are associated with investment advisers or broker-dealers.

Gupta has filed a complaint in this Court seeking to enjoin the SEC's administrative proceeding, alleging that (1) the proceeding includes a claim for civil penalties that would have been available only in a federal district court until passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") on July 21, 2010, and (2) the SEC is violating his due process rights because the administrative proceeding does not provide a right to trial by jury or the same discovery rights as courts provide and the SEC has brought all other Rajaratnam-related claims in district court.

Gupta is essentially seeking to convert potential factual, legal, and constitutional defenses to an administrative proceeding into a claim that he is entitled to immediate interlocutory review of the OIP in a district court. But there are fundamental flaws in Gupta's attempt to seek review

now. Those flaws preclude Gupta from relying on the Administrative Procedure Act's ("APA") limited waiver of sovereign immunity. 5 U.S.C. 702. The APA provides for review only from final agency actions, and an order instituting proceedings is not a final agency action. 5 U.S.C. 704; *FTC v. Standard Oil Co. of Cal.*, 449 U.S. 232 (1980). In addition, under the APA, the proper form of proceeding for judicial review of agency action is "the special statutory review proceeding relevant to the subject matter." 5 U.S.C. 703. Here, the federal securities laws provide for judicial review of administrative proceedings in a United States courts of appeals after the SEC enters a final order. *See* 15 U.S.C. 77i(a); 15 U.S.C. 78y(a); 15 U.S.C. 80b-13(a); 15 U.S.C. 80a-42(a).

Although courts have, in very limited situations, allowed challenges to agency action outside of special statutory review proceedings provided by Congress—such as where the agency is either statutorily barred from taking the action it has taken, or does not have the power to grant the relief sought by the plaintiff—none has allowed it in the circumstances here. Indeed, the types of potential defenses Gupta seeks to raise—including his Constitutional claims—are routinely decided by administrative agencies. Consequently, the federal courts have consistently rejected collateral attacks on agency proceedings raising such claims.

Moreover, Gupta's claims cannot proceed because they are not ripe for judicial review and the exhaustion doctrine dictates that he proceed first in the administrative proceeding. Gupta's retroactivity claim in particular will not be ripe unless and until there has been a finding that he engaged in insider trading and a decision that penalties under the provisions added by Dodd-Frank are warranted. Although Gupta characterizes his retroactivity claim as a strictly legal and collateral issue entitled to immediate review, it is indistinguishable from the myriad of other legal issues that agencies conducting administrative proceedings are routinely required to

address. Requiring exhaustion is also appropriate for Gupta's remaining claims because they need not be addressed by a court before or while the SEC considers them. If the SEC finds that Gupta did not engage in insider trading or otherwise decides not to impose any sanctions on Gupta, there will be no need for judicial review of these issues. If the SEC does find he has engaged in insider trading, a court of appeals can then review all of Gupta's claims in light of the SEC's final determination on those claims.

As to Gupta's failure to state a claim: it is axiomatic that to state a claim for injunctive relief he must allege the absence of an adequate remedy at law. Gupta cannot do so as the Congressionally-prescribed judicial review provisions provide an adequate remedy because, to the extent he is dissatisfied with a final order of the SEC, he may obtain judicial review in a court of appeals.

BACKGROUND

On March 1, 2011, the SEC issued its Order Instituting Public Administrative and Cease-and-Desist Proceedings Pursuant to Section 8A of the Securities Act of 1933 [15 U.S.C. 77h-1], Sections 15(b) and 21C of the Securities Exchange Act of 1934 [15 U.S.C. 78o(b) & 78u-3], Section 203(f) of the Investment Advisers Act of 1940 [15 U.S.C. 80b-3(f)], and Section 9(b) of the Investment Company Act of 1940 [15 U.S.C. 80a-9(b)]. Exhibit 1 hereto. Each of the statutes listed in the title of the OIP authorizes the SEC to issue an order, after notice and opportunity for hearing, imposing a sanction if the SEC finds the respondent has engaged in the violations prohibited by the statute and it is in the public interest to impose the sanction. Dodd-Frank did not alter the basic grant of authority to the SEC to institute these administrative proceedings.

The OIP lists the remedial actions the SEC may consider entering if it finds that the allegations presented in the OIP are substantiated. The federal securities laws authorized the SEC to impose most of these remedial actions even before Dodd-Frank was enacted. The following chart shows the limited impact of Dodd-Frank on the potential sanctions.

Authority for Instituting AP	**Relief Requested**	**Dodd-Frank Impact, If Any**
Section 8A of the Securities Act	cease and desist order – 8A(a)	no change
	disgorgement – 8A(e)	no change
	civil penalties – 8A(g)	added by Dodd-Frank § 929P
	officer and director bar – 8A(f)	no change
Section 15(b) of the Exchange Act	disgorgement – 21B(a)(1)	no change
	civil penalties – 21B(e)	no change
Section 21C of the Exchange Act	cease and desist order – 21C(a)	no change
	disgorgement – 21C(e)	no change
	civil penalties – 21B(a)(2)	added by Dodd-Frank § 929P
	officer and director bar – 21C(f)	no change
Section 203(f) of the Investment Adviser Act	civil penalties – 203(i)	no change (Dodd-Frank added penalties for 203(k) actions, but OIP does not include such a claim)
Section 9(b) of the Investment Company Act	civil penalties – 9(d)	no change (Dodd-Frank added penalties for 9(f) actions, but OIP does not include such a claim)

The SEC's Rules of Practice set forth the procedures governing the proceeding against Gupta. *See* 17 C.F.R. 201.100, *et seq.* Those procedures provide, among other things, that Enforcement must make available to any party documents (other than privileged documents) obtained in the investigation leading to Enforcement's recommendation to institute the proceedings soon after the OIP is served. 17 C.F.R. 201.230. In addition, a respondent may request the issuance of both document and testimony subpoenas to obtain additional information.

17 C.F.R. 201.232. The rules also provide a procedure for seeking summary disposition that can be used if there are legal issues that can be resolved without a hearing. 17 C.F.R. 201.250. And the hearing officer—an administrative law judge ("ALJ")—can certify issues for interlocutory review by the Commission (*i.e.*, the five Commissioners who are the head of the SEC) if a "ruling involves a controlling issue of law as to which there is substantial ground for difference of opinion" and "an immediate review of the order may materially advance the completion of the proceeding." 17 C.F.R. 201.400(c). At hearings, while the SEC has not adopted the Federal Rules of Evidence, the Rules of Practice provide that the hearing officer "shall exclude all evidence that is irrelevant, immaterial or unduly repetitious." 17 C.F.R. 201.320. Gupta will have an opportunity to cross examine all of Enforcement's witnesses and to present his own evidence. Following a hearing, the hearing officer issues an initial decision, and any party may seek review of that decision by the Commission. 17 C.F.R. 201.410.[1]

As noted above, the Securities Act, the Exchange Act, the Investment Advisers Act, and the Investment Company Act all provide that final SEC decisions are subject to review in a court of appeals. For example, Section 25(a)(1) of the Exchange Act provides in relevant part that:

> A person aggrieved by a final order of the Commission entered pursuant to this chapter may obtain review of the order in the United States Court of Appeals for the circuit in which he resides or has his principal place of business, or for the District of Columbia Circuit, by filing in such court, within sixty days after the entry of the order, a written petition requesting that the order be modified or set aside in whole or in part.

15 U.S.C. 78y(a)(1); *see also* 15 U.S.C. 77i(a); 15 U.S.C. 80b-13(a); 15 U.S.C. 80a-42(a). Section 25 also prescribes a comprehensive process for review of final SEC orders as it (1)

[1] The Supreme Court has recognized that the fact that a hearing officer rather than a jury makes findings of fact in an administrative proceeding does not violate the Seventh Amendment, even if civil penalties may be imposed in the proceeding. *See generally Atlas Roofing Co. v. Occupational Safety and Health Review Commission*, 430 U.S. 442 (1977). Additionally, the Second Circuit has found that SEC administrative proceedings meet the standards of due process. *Sinclair v. SEC*, 444 F.2d 399, 401-02 (2d Cir. 1971).

identifies what constitutes the record before the agency, (2) provides the scope of review, (3) explains the relief available, (4) provides for supplemental proceedings before the Commission if necessary to adduce additional evidence or make additional findings, (5) addresses whether stays pending appeal are available and (6) requires exhaustion of administrative remedies before the SEC. *See generally* 15 U.S.C. 78y(a) and (c).

At present, the SEC's proceeding against Gupta has not resulted in a final order. The evidentiary hearing is scheduled to commence on July 18, 2011. At this point Gupta has not raised before the ALJ either his due process or his retroactivity arguments. However, the ALJ overseeing the case has informed the parties that she will consider any remedy arguments in briefing that will be submitted after this hearing. The ALJ declined to rule on the retroactivity issue before the hearing because she found it would not make sense to issue an advisory opinion on sanctions before she determined whether Enforcement had met its burden of proving that Gupta had committed the violations of the securities laws alleged in the OIP. *See* Exhibit 2 hereto (excerpt of transcript of March 21, 2011 prehearing conference in *In the Matter of Rajat K. Gupta*).

ARGUMENT

I. Gupta Cannot Show Any Statutory Basis for Asserting Jurisdiction.

The United States "as sovereign, is immune from suit save as it consents to be sued." *United States v. Sherwood*, 312 U.S. 584, 586 (1941). Consent to being sued is a requirement for federal subject matter jurisdiction over a claim against federal agencies, including the SEC. *See FDIC v. Meyer*, 510 U.S. 471, 475 (1994); *American Benefits Group, Inc. v. NASD*, 1999 U.S. Dist. LEXIS 12321, at *10 (S.D.N.Y. Aug. 10, 1999). An agency may be sued only in those limited circumstances where there has been an express Congressional waiver of sovereign

immunity, and then only in the specific manner that Congress has provided. *United States v. Dalm*, 494 U.S. 596, 608 (1990). Therefore, the "conditions upon which the Government consents to be sued must be strictly observed and exceptions thereto are not to be implied." *Lehman v. Nakshian*, 453 U.S. 156, 161 (1981); *see also Lunney v. United States*, 319 F.3d 550, 554 (2d Cir. 2003) ("[s]overeign immunity is a jurisdictional bar, and a waiver of sovereign immunity is to be construed strictly and limited to its express terms").

Nowhere does Gupta cite any valid basis for a district court to exercise original jurisdiction here. Although he recites a medley of statutes in his Complaint (at ¶ 3), none of these provisions—including 28 U.S.C. 1331, 1337, 1346, 1361 and 2201, and 5 U.S.C. 702—supports jurisdiction in the circumstances.

A. None of the General Jurisdictional Provisions Gupta Cites Waives Sovereign Immunity.

Under 28 U.S.C. 1331, district courts have jurisdiction over claims "arising under" the Constitution, laws, or treaties of the United States. Likewise, 28 U.S.C. 1337 grants district courts jurisdiction over claims "arising under" federal statutes pertaining to commerce and trade.[2] However, neither provision waives sovereign immunity to permit suits against federal agencies.[3]

Gupta's reliance on 28 U.S.C. 1346 is similarly misplaced. Section 1346 contains both the Federal Tort Claims Act ("FTCA"), 28 U.S.C. 1346(b), and the Little Tucker Act,

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[2] *See, e.g., Franchise Tax Bd. of State of Cal. v. Construction Laborers Vacation Trust for Southern Cal.*, 463 U.S. 1, 8 n.7 (1983) ("we have not distinguished between the 'arising under' standards of §1337 and §1331").

[3] *See, e.g., Mack v. United States*, 814 F.2d 120, 122 (2d Cir. 1987) ("[28 U.S.C. 1331] does not constitute a waiver of sovereign immunity"); *CETA Workers' Action Comm. v. City of New York*, 1978 U.S. Dist. LEXIS 16266, at *18 (S.D.N.Y. Jul. 31, 1978) ("it is clear [28 U.S.C. 1337] contains no express waiver of sovereign immunity").

1346(a)(2). Both the FTCA[4] and the Little Tucker Act[5] would waive sovereign immunity only if Gupta were seeking "money damages" from the United States. Because Gupta seeks only declaratory and injunctive relief, those provisions are inapplicable.[6]

Gupta's contention that this Court has jurisdiction under the Mandamus Statute, 28 U.S.C. 1361, is also baseless, as it does not waive sovereign immunity.[7] Similarly, he reliance on the Declaratory Judgment Act, 28 U.S.C. 2201 ("DJA") is misplaced as it DJA also does not waive sovereign immunity.[8]

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[4] *See Kosak v. United States*, 465 U.S. 848, 852 n.7 (1984) ("[FTCA] permits recovery only of money damages") (internal quotation marks omitted); *Makarova v. United States*, 201 F.3d 110, 113 (2d Cir. 2000) ("The FTCA waives the government's sovereign immunity only for: claims against the United States for money damages . . .") (internal quotation marks omitted).

[5] *See Martin v. Hidalgo*, 1980 U.S. Dist. LEXIS 15290, at *6-7 (S.D.N.Y. Dec. 1, 1980) (Little Tucker Act "waive[s] . . . sovereign immunity for claims for money against the United States"); *Greene v. United* States, 222 F. Supp. 2d 198, 200 (D. Conn. 2002) (Little Tucker Act "provides a limited waiver of sovereign immunity for non-tort damages claims against the United States").

[6] *See Trackwell v. United States*, 472 F.3d 1242, 1244 (10th Cir. 2007) (Little Tucker Act "authorizes suits for money damages against the United States" but "does not waive sovereign immunity for . . . equitable claims").

[7] *See Doe v. Civiletti*, 635 F.2d 88, 94 (2d Cir. 1980) ("Nor is the mandamus statute an all-purpose waiver of the Government's immunity from suit."); *Estate of Arthur K. Watson v. Blumenthal*, 586 F.2d 925, 935 (2d Cir. 1978) ("The mandamus statute is simply not a generalized waiver of the sovereign's immunity.").

[8] *See Muirhead v. Mecham*, 427 F.3d 14, 17 n.1 (1st Cir. 2005) (DJA "plainly does not operate as an express waiver of sovereign immunity"); *Wyoming v. United States*, 279 F.3d 1214, 1225 (10th Cir. 2002) (DJA does not waive sovereign immunity); *Anderson v. United States*, 229 F.2d 675, 677 (5th Cir. 1956) (DJA "does not grant any consent to the United States to be sued") (citations omitted); *Serra v. United States GSA*, 667 F. Supp. 1042, 1051 n.4 (S.D.N.Y. 1987), *aff'd*, 847 F.2d 1045 (2d Cir. 1988) (DJA "does not waive sovereign immunity").

B. The APA Does Not Waive the SEC's Sovereign Immunity in this Matter.

Gupta cites APA Section 702, 5 U.S.C. 702, as a basis for this Court to exercise jurisdiction over his claims. *See* Complaint ¶ 3. APA Section 702 provides, in relevant part, that:

> [a] person suffering legal wrong because of agency action, or adversely affected or aggrieved by agency action within the meaning of a relevant statute, is entitled to judicial review thereof. . . . Nothing herein (1) affects other limitations on judicial review or the power or duty of the court to dismiss any action or deny relief on any other appropriate legal or equitable ground . . . .

Because Section 702 specifically preserves existing limits on judicial review, it does not waive sovereign immunity when restrictions on review exist. *Sprecher v. Graber*, 716 F.2d 968, 974 (2d Cir. 1983). Those restrictions include that review under the APA is limited to final agency action and must occur through special statutory review provisions established by statute. *See* 5 U.S.C. 703, 704.

1. The SEC's decision to institute an administrative proceeding against Gupta is not reviewable under the APA because it is not final agency action.

Under the APA, a court may only review "final agency action." 5 U.S.C. 704. "This requirement of finality is jurisdictional." *Air Espana v. Brien*, 165 F.3d 148, 152 (2d Cir. 1999). Whether an agency action is "final" turns on whether the action (1) "mark[s] the consummation of the agency's decisionmaking process—it must not be of a merely tentative or interlocutory nature," and (2) is an action "by which rights or obligations have been determined, or from which legal consequences will flow." *Bennett v. Spear*, 520 U.S. 154, 178 (1997) (internal quotation marks and citations omitted).

Gupta's Complaint does not identify *any* "final agency action" for this Court to review—nor could it—as the Supreme Court has foreclosed any argument that the SEC's OIP is a final agency action. In *FTC v. Standard Oil Co. of Cal.*, 449 U.S. 232 (1980) ("*SoCal*"), the Supreme

Court ruled unanimously that an agency's decision to institute administrative proceedings is not sufficiently "final" under the APA to warrant judicial review. The FTC's initiating complaint in *SoCal*—like the SEC's OIP here—serves "only to initiate the proceedings" and has "no legal force or practical effect" on the respondent until the matter is adjudicated before an ALJ. *Id.* at 242-43. According to *SoCal*, premature judicial review of interlocutory administrative measures is "likely to interfere with the proper functioning of [an] agency" and create a "burden for the courts," as it "denies the agency an opportunity to correct its own mistakes and to apply its expertise . . . [and] leads to piecemeal review which at the least is inefficient and upon completion of the agency process might prove to have been unnecessary." *Id.* at 242. In reaching this conclusion, the Supreme Court specifically rejected the argument that the expense and disruption associated with being a respondent in an administrative proceeding justified immediate judicial review. *Id.* at 242-43. The Supreme Court explained that these burdens are no different than the "disruptions that accompany any major litigation." *Id.* According to the Court, "'[m]ere litigation expense, even substantial and unrecoupable cost, does not constitute irreparable injury'" so as to warrant immediate judicial review of an agency's interlocutory decisions. *Id.* (quoting *Renegotiation Bd. v. Bannercraft Clothing, Inc.*, 415 U.S. 1, 24 (1974)).

In the present case, as in *SoCal*, the SEC has decided nothing other than to initiate an administrative proceeding. As was the case in *SoCal*, the SEC's OIP "represents a threshold determination that further inquiry is warranted and that a complaint should initiate proceedings." *Id.* at 241. The SEC has not issued any final decisions regarding the retroactive application of Section 929P of Dodd-Frank, nor has it addressed any due process, equal protection or other claims Gupta may raise in the future. At this point, Enforcement bears the burden of showing that its allegations are meritorious. 17 C.F.R. 201.300, 201.301. If the Commission ultimately

enters an order finding that Gupta violated the federal securities laws and imposing a sanction, that order would be "final" under the APA, and subject to review by a United States court of appeals. *See* 15 U.S.C. 77i(a); 15 U.S.C. 78y(a). Gupta must await that final action before seeking judicial review.

2. Courts of appeals have exclusive jurisdiction to review orders entered in SEC administrative proceedings.

Gupta also cannot bring any of his claims under the APA because the APA and federal securities laws together establish that review of any aspect of an administrative proceeding is available only in a United States court of appeals after the administrative proceeding is complete.

Section 703 of the APA states that "the form of proceeding for judicial review is the special statutory review proceeding relevant to the subject matter in a court specified by statute." 5 U.S.C. 703. The federal securities laws prescribe a review proceeding for SEC administrative proceedings.[9] Section 25(a) of the Exchange Act, 15 U.S.C. 78y(a), which explicitly vests jurisdiction in courts of appeals, "provides the specific review proceeding" prescribed in Section 703 for seeking judicial review of Commission actions. *American Benefits*, 1999 U.S. Dist. LEXIS 12321, at *12. Just last month, in *Altman v. SEC*, the court dismissed an action seeking declaratory and injunctive relief filed by an individual challenging a disciplinary sanction imposed upon him in an SEC administrative proceeding and seeking a stay of further SEC proceedings against him. __ F. Supp. 2d __, 2011 U.S. Dist. LEXIS 23230 (S.D.N.Y. Mar. 8, 2011) (Holwell, J.). The court held that Section 25(a), requires a plaintiff to seek relief from a court of appeals:

> The SEC contends that Section 78y(a)(1) requires that Altman bring any action challenging his sanction, based on constitutional arguments or otherwise, in the Court of Appeals. They are correct. "The Court of Appeals for the Second

[9] *See* 15 U.S.C. 78y(a)(1) (quoted at page 5, *supra*); *see also* 15 U.S.C. 77i(a); 15 U.S.C. 80a-42(a); 15 U.S.C. 80b-13(a).

> Circuit has held that generally under the Exchange Act 'a litigant is required to pursue all of his administrative remedies before he will be permitted to seek judicial relief.'" *American Benefits Grp., Inc. v. Nat'l Ass'n of Securities Dealers*, No. 99 Civ. 4733, 1999 WL 605246 at *5 (S.D.N.Y. Aug. 10, 1999) (*quoting Touche Ross Co. v. Securities and Exchange Commission*, 609 F.2d 570, 574 (2d Cir. 1979)). The Exchange Act allows those aggrieved by SEC orders or rules to bring challenges in a United States Court of Appeals. 15 U.S.C. §78y(a)(1), (b)(1). Those courts' jurisdiction is exclusive. 15 U.S.C. §78y(a)(3), (b)(3).

2011 U.S. Dist. LEXIS 23230, at *9-10.[10] The *Altman* court noted that not only did district courts lack jurisdiction to hear post-enforcement challenges to SEC administrative proceedings because the jurisdiction of the court of appeals is exclusive, but that the "same is true regarding ongoing or pre-enforcement disciplinary proceedings." *Id*. at *10. The court continued "the fact that a plaintiff raises a constitutional challenge to SEC rules does not alter the analysis or application of" the special statutory review provision; the fact "that a plaintiff's constitutional claims can be meaningfully addressed in the Court of Appeals trumps other considerations." *Id.* at *12-13, 21 (citations and quotations omitted). Because the federal securities laws provide for judicial review of SEC administrative proceedings in a court of appeals at the conclusion of administrative proceedings, and that review can adequately address Gupta's claims, he cannot seek relief in this court at this time.

II. Gupta Has No Other Basis for Jurisdiction.

None of the limited circumstances in which a plaintiff may obtain judicial relief outside of the special statutory review provisions applicable to SEC administrative proceedings applies to this case. In *Thunder Basin Coal Co. v. Reich*, 510 U.S. 200 (1994), the Supreme Court ruled

[10] Similarly, in *Pierce v. SEC*, 737 F. Supp. 2d 1068 (N.D. Cal. 2010), Pierce filed a complaint in district court seeking to enjoin an administrative proceeding against him. The district court relied upon Section 25(a) and noted that "the federal securities laws provide that judicial review is vested in the Courts of Appeal." *Id*. at 1072. The court dismissed the complaint, concluding that "because Congress has established a specific statutory system for judicial review of SEC actions by the Court of Appeals, Pierce cannot rely on the APA's general review provisions as a source of jurisdiction." *Id*. at 1073.

that the special statutory review scheme "prevents a district court from exercising subject matter jurisdiction over a pre-enforcement challenge." *Id*. at 202. This is the rule. The few exceptions to it are both limited and narrow, and none applies here.

Just like Gupta, the plaintiffs in *Thunder Basin* sought an injunction to prevent an agency enforcement proceeding, including a potential hearing before an ALJ and possible civil penalties. 510 U.S. at 202, 207-208. Just like Gupta, they claimed that proceeding through the special statutory review process would violate their due process rights. *Id.* at 214. The Supreme Court found this claim unavailing, holding that the plaintiffs had to make those arguments before the agency and then in a court of appeals. *Id.* at 214-215. The same is true for Gupta.

A. The *Free Enterprise* Exception Does Not Grant District Courts Jurisdiction to Enjoin Ongoing Agency Proceedings.

Less than a year ago the Supreme Court reaffirmed the *Thunder Basin* principle that district courts typically lack jurisdiction to hear cases when a statute directs review to a court of appeals, finding that "[g]enerally, when Congress creates procedures designed to permit agency expertise to be brought to bear on particular problems, those procedures are to be exclusive." *Free Enterprise Fund v. PCAOB*, 130 S. Ct. 3138, 3150 (2010) (citations and quotations omitted). The narrow exception the Supreme Court set forth in *Free Enterprise* is an extraordinarily difficult one to satisfy. The Court recognized that district courts may have jurisdiction if "a finding of preclusion could foreclose all meaningful judicial review; if the suit is wholly collateral to a statute's review provisions; and if the claims are outside the agency's expertise." *Id.* at 3150 (citations and quotations omitted). In this case, each of the three factors the Supreme Court identified shows that Gupta must rely on the review procedures established by Congress in the federal securities laws.

1. Gupta can obtain meaningful judicial review in a court of appeals.

At the conclusion of the administrative proceedings before the SEC, Gupta can, if he is dissatisfied with the outcome, challenge the result in a court of appeals, where all of his claims, including "statutory and constitutional claims . . . can be meaningfully addressed." *Thunder Basin*, 510 U.S. at 215. Unlike *Free Enterprise*, where the plaintiffs could only be assured of judicial review under the statutory scheme by challenging a random rule proposal with no direct relation to their claim, this case does not implicate the "serious constitutional question that would arise if an agency statute were construed to preclude all judicial review." *Thunder Basin*, 510 U.S. at 215 n.10 (citations and quotations omitted); *see also FCC v. ITT World Communications Inc.*, 466 U.S. 463, 468 (1984) (holding that district court lacked subject matter jurisdiction because the plaintiffs "may not evade [special statutory review] provisions by requesting the District Court to enjoin action that is the outcome of the agency's order"); *Altman v. SEC*, 2011 U.S. Dist. LEXIS 23230, at *21 (plaintiff's constitutional claims can be meaningfully addressed in a court of appeals).

Additionally, because Gupta can obtain judicial review in a court of appeals, he fails this circuit's test for district court jurisdiction over claims against agencies. The Second Circuit has ruled that special review statutes "that vest judicial review of administrative orders exclusively in the courts of appeals also preclude district courts from hearing claims that are inescapably intertwined with review of such orders." *Merritt v. Shuttle, Inc.*, 245 F.3d 182, 187 (2d Cir. 2001) (Sotomayor, J.) (citations and quotations omitted). In *Merritt*, the Second Circuit ruled that district courts cannot hear a claim that "alleges that the plaintiff was injured by [an agency] order" when "the court of appeals has authority to hear the claim on direct review of the agency

order." 245 F.3d at 187. Here Gupta is trying to do exactly what *Merritt* forbade: to use collateral litigation to attack the SEC's OIP. *See id.* at 188.

2. Gupta's claims are not "wholly collateral" to the review provisions.

Gupta also fails the second part of the *Free Enterprise* test, as his claims are not "wholly collateral" to the statutory review provisions, but rather "inescapably intertwined" in an agency administrative proceeding that is fully embedded in the statutory review scheme. *See Merritt*, 245 F.3d at 187 (finding that a claim is inescapably intertwined where it alleges injury from an order and the court of appeals can hear the claim on direct review). The *Free Enterprise* plaintiffs were bringing a facial constitutional challenge to a statute unrelated to any allegation that they violated any law or regulation. Gupta, however, has already been alleged to have committed multiple violations of the federal securities laws and can raise all of his claims in the ongoing proceeding against him.

Notably, when the Supreme Court used the term "wholly collateral," it did not mean collateral to a particular agency ruling or potential ruling but, rather, collateral to the entirety of the statutory review scheme. Gupta's argument that the retroactivity issue is collateral to the other issues in the administrative proceeding falls flat. The SEC's imposition of sanctions for violations of the federal securities law in an administrative proceeding is not collateral to the statutory review scheme for final orders of the agency; rather, it is an integral part to the scheme.

To artificially pull out of the administrative proceeding a single potential issue that is inexorably intertwined with the entire administrative proceeding defeats the policy underlying letting agencies develop their own record and rulings. Such "[j]udicial intervention into the agency process denies the agency an opportunity to correct its own mistakes and to apply its expertise . . . [and] leads to piecemeal review which at the least is inefficient and upon completion of the agency process might prove to have been unnecessary." *United States ex rel.*

St. Regis Mohawk Tribe v. President R.C.-St. Regis Mgmt. Co., 451 F.3d 44, 50 (2d Cir. 2006) (quoting *SoCal*, 449 U.S. at 242). If this Court found any of Gupta's claims to be "wholly collateral," then any time a respondent in an administrative proceeding contends that the agency is biased or is violating his due process rights—defenses routinely asserted in administrative proceedings—he will be able to do an end-run around the special statutory review provisions and file a claim in district court. Indeed, Gupta's claim is directly analogous to the plaintiff's claim in *Thunder Basin*, where the Supreme Court explicitly found that the district court lacked jurisdiction. 510 U.S. at 216.

Gupta fares no better under the exception recognized by the Second Circuit in *Touche Ross & Co. v. SEC*, 609 F.2d 570 (2d Cir. 1979). Although in *Touche Ross* the Second Circuit found that the district court had subject matter jurisdiction, that jurisdiction was limited to the specific issue of "whether the Commission has the Authority to promulgate Rule 2(e) and to proceed thereunder."[11] 609 F.2d at 574. The court explicitly rejected arguments that the district court had jurisdiction to hear the *Touche Ross* plaintiffs' other claims, which are directly analogous to Gupta's:

> appellants must exhaust their administrative remedies before the SEC prior to attempting to obtain judicial review of their other claims, *including their claim that the Commission is acting with bias and will not afford them a fair hearing in accordance with due process.*

Id. at 582 (emphasis added). Thus, any due process claim by Gupta must first be made before the agency, and then to a court of appeals.

[11] Even this claim would not likely satisfy the more recent, and substantially narrower, *Free Enterprise* test.

3. Determining whether a person has violated the securities laws and what sanction should result is within the SEC's expertise.

Gupta also cannot demonstrate that the issues he raises in district court are beyond the SEC's expertise. This case is easily distinguishable from *Free Enterprise*, where the plaintiffs argued that the statute establishing the PCAOB violated constitutional principles of separation of powers and the Appointments Clause. As the SEC lacked the power to declare the PCAOB unconstitutional, the SEC could not grant them the relief they sought. *See Altman*, 2011 U.S. Dist. LEXIS 23230 at *11-15 (distinguishing Altman's attempts to enjoin SEC administrative proceeding from the *Free Enterprise* plaintiffs' claims). The Second Circuit's test for whether a district court can hear agency cases is also compelling here: "whether the administrative agency ha[s] the authority to decide the issue raised by the claim." *Merritt*, 245 F.3d at 188 n.9 (citations and quotations omitted). If the agency can decide the issue and grant the relief, then the district courts do not have jurisdiction.

In the administrative proceeding, the SEC (through the ALJ and/or the Commissioners themselves) has the power to provide relief to Gupta if his claims have any merit. The SEC has the power to (1) dismiss these proceedings, (2) grant summary disposition in Gupta's favor, (3) determine that he committed no violations, (4) determine that no civil penalties are appropriate for any violations he may have committed, and/or (5) determine that only civil penalties under statutory provisions existing prior to the enactment of Dodd-Frank should be applied to conduct occurring before that law was passed. Significantly, the SEC has explicitly ruled upon the propriety of retroactive applications of statutes in administrative proceedings.[12] *Cf. Thunder*

[12] *See, e.g., In the Matter of Castle Securities Corp. and Michael T. Studer*, 2004 SEC LEXIS 154, at *24-25 (Jan. 23, 2004) (ALJ refused to impose one form of sanction for violations of federal securities laws because it would be impermissibly retroactive); *In the Matter of Laurie Jones Canady*, 54 S.E.C. 65, 87 (1999) (Opinion of the Commission rejecting argument that a sanction was an impermissible retroactive application of a statute); *In the Matter of Carroll A.*

Basin, 510 U.S. at 214 n.17, n.18 (finding the fact that agency had addressed claims previously showed its expertise on issue).

As Gupta fails each part of the *Free Enterprise* test and has an adequate remedy in seeking judicial review of any final SEC order in a court of appeals, this Court lacks subject matter jurisdiction under *Free Enterprise*, *Thunder Basin*, and *Merritt*.

B. Gupta Cannot Demonstrate that the SEC Is Acting *Ultra Vires* Under *Leedom v. Kyne*.

The Supreme Court has said that district courts can enjoin *ultra vires* agency action—but only where that action is taken in violation of a "definite prohibition" in a statute. *Leedom v. Kyne*, 358 U.S. 184, 189 (1958). Gupta has not alleged, nor could he, any "definite prohibition" in any statute that the SEC violated by instituting proceedings against him. This is fatal to any *ultra vires* claim as the Second Circuit has said that the "extremely narrow" exception to statutory review provisions in *Leedom* "applies only where the [agency] has clearly violated an express provision of the statute." *Goethe House New York v. NLRB*, 869 F.2d 75, 77-78 (2d Cir. 1989).

Although Gupta asserts that the SEC cannot retroactively apply certain provisions of Dodd-Frank as they relate to civil penalties, this potential legal issue is far from sufficient to demonstrate *ultra vires* action. First—and critically—the SEC has not even retroactively applied the provisions against Gupta. Rather, it has given him notice in the OIP that it will consider applying these penalty provisions against him. Only if Gupta is found to have violated the federal securities laws would the application of these provisions be at issue. And if that occurs,

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Wallace, CPA, 56 S.E.C. 865, 868 (2003) (Opinion of the Commission considering and rejecting argument that amendment to rule was impermissibly applied retroactively); *In the Matter of Barry C. Scutillo, CPA*, 2001 SEC LEXIS 844, at *68 (May 3, 2001) (ALJ initial decision considering and rejecting argument that amendment to rule was impermissibly applied retroactively).

Gupta will have the opportunity to convince the SEC not to apply them because of retroactivity or other concerns. Only if the SEC were to impose sanctions under those new penalty provisions would Gupta even have a claim that the SEC had acted in violation of the law. But even then, he could not meet the *Leedom* test as there is no "definite prohibition" in the statute.

The impropriety of the relief that Gupta seeks is highlighted by the fact that he asks this Court to enjoin the SEC's entire proceeding against him when only a small part of it even potentially implicates claimed retroactivity issues. As explained in the Background section above, most of the relief being sought in the proceeding, including civil monetary penalties under the Investment Advisers Act, the Investment Company Act, and Section 15(b) of the Exchange Act, could be imposed in an administrative proceeding before the enactment of Dodd-Frank.

III. The Doctrines of Ripeness and Exhaustion Bar Gupta's Claims.

A. Gupta's Claims Are Not Ripe for Review.

Even if Gupta could overcome the jurisdictional deficiencies described above, his claims are not ripe for review. "The ripeness doctrine is drawn both from Article III limitations on judicial power and from prudential reasons for refusing to exercise jurisdiction." *New York Civil Liberties Union v. Grandeau*, 528 F.3d 122, 130 (2d Cir. 2008) (quoting *National Park Hospitality Ass'n v. Dep't of Interior*, 538 U.S. 803, 808 (2003) (internal quotations marks omitted)).

In the context of administrative proceedings, the Supreme Court has explained that the ripeness requirement is designed "[t]o prevent the courts, through avoidance of premature adjudication, from entangling themselves in abstract disagreements over administrative policies, and also to protect the agencies from judicial interference until an administrative decision has been formalized and its effects felt in a concrete way by the challenging parties." *Abbott Lab. v.*

Gardner, 387 U.S. 136, 148-49 (1967) (overruled and superseded on other grounds). "The ripeness doctrine reflects a judgment that the disadvantages of a premature review . . . ordinarily outweigh the additional costs of—even repetitive—post-implementation litigation." *Ohio Forestry Ass'n. v. Sierra Club*, 523 U.S. 726, 735 (1998).

In determining whether a challenge to administrative action is ripe for judicial review, courts employ a "two-step inquiry" that is "relevant for both constitutional and prudential ripeness analysis." *New York Civil Liberties Union*, 528 F.3d at 132 n.9. Courts are required "to evaluate both the fitness of the issues for judicial decision and the hardship to the parties of withholding court consideration." *Id.* at 132 (quoting *Abbott Lab.*, 387 U.S. at 149).

The SEC has not ruled against Gupta, has not determined that Section 929P of Dodd-Frank can be applied retroactively, and has not imposed any penalties. The retroactivity issue will be moot if Enforcement cannot prove that Gupta violated the federal securities laws or that penalties are warranted. If the SEC does determine that Enforcement has proven that Gupta committed securities laws violations and that penalties are appropriate, it will consider any retroactivity issues Gupta raises before finally imposing penalties. And as Gupta's own complaint emphasizes, one of the five Commissioners has publicly discussed her concerns about applying Dodd-Frank retroactively (Complaint ¶ 13). Thus it would be premature for this Court to address this issue, making Gupta's claim unfit for judicial review.

Nor will Gupta suffer any present hardship if this Court does not consider his claim. In this context, "hardship" means "adverse effects of a strictly legal kind," for example, a command to do or to refrain from doing something or an imposition of liability. *Ohio Forestry*, 523 U.S. at 733. "The mere possibility of future injury, unless it is the cause of some present detriment, does not constitute hardship." *New York Civil Liberties Union*, 528 F.3d at 134 (quoting *Simmonds v.*

INS, 326 F.3d 351, 360 (2d Cir. 2003)). Because the SEC has not made any determination about whether Gupta violated any securities laws and has not imposed any sanction, Gupta does not have any legally cognizable hardship. Gupta's argument that a decision by this Court will reduce or eliminate his litigation costs in the administrative proceeding (Complaint ¶ 18) is unavailing; the Supreme Court "has not considered this kind of litigation cost saving sufficient by itself to justify review in a case that would otherwise be unripe." *Ohio Forestry Ass'n*, 523 U.S. at 735.

B. Gupta Has Failed to Exhaust His Administrative Remedies.

"As a rule, plaintiffs must exhaust administrative remedies before seeking redress in federal court." *Skubel v. Fuoroli*, 113 F.3d 330, 334 (2d Cir. 1997) (citing *Pavano v. Shalala*, 95 F.3d 147, 150 (2d Cir.1996)). "[T]he long settled rule of judicial administration [is] that no one is entitled to judicial relief for a supposed or threatened injury until the prescribed administrative remedy has been exhausted." *Myers v. Bethlehem Shipbuilding Corp.*, 303 U.S. 41, 50-51 (1938). The primary purpose of this rule is "the avoidance of premature interruption of the administrative process," *McKart v. United States*, 395 U.S. 185, 193 (1960), an objective that Gupta is attempting to undermine.

This obligation to exhaust administrative remedies is especially compelling when, as is the case here, a respondent is attempting to enjoin an administrative proceeding that the SEC is authorized under the federal securities laws to institute. Indeed,

> [n]umerous courts have rejected similar efforts to enjoin SEC administrative proceedings, and held that parties must exhaust administrative remedies prior to seeking judicial review, including when the party seeking the injunction claims that the administrative proceedings violate due process. *See SEC v. R.A. Holman & Co.*, 323 F.2d 284, 287 (D.C. Cir. 1963) (reversing district court order enjoining SEC administrative proceeding because administrative remedies not exhausted; plaintiff claimed due process violation and that SEC Commissioner should be disqualified); *Wolf Corporation v. SEC*, 317 F.2d 139, 142 (D.C. Cir. 1963) (upholding refusal to enjoin SEC's stop order proceeding against issuer's proposed securities registration, and holding that claims relating to evidence

> allegedly seized in violation of the Fourth Amendment and challenges to the Commission's authority must first be made to the Commission); *First Jersey Sec. Inc. v. SEC*, 553 F. Supp. 205, 208-09 (D.N.J. 1982) (refusing to enjoin SEC administrative proceedings, where plaintiff alleged various constitutional and statutory violations because Second Circuit precedent mandates that "the procedures established for review of SEC actions deprive this court of jurisdiction over suits that seek to interrupt the agency proceedings").

Pierce v. SEC, 737 F. Supp. 2d 1068, 1075-76 (N.D. Cal. 2010) (dismissing action for lack of jurisdiction given plaintiff's failure to exhaust administrative remedies); *see also In re SEC ex rel. Glotzer*, 374 F.3d 184, 192 (2d Cir. 2004) (issuing writ of mandamus where district court lacked subject matter jurisdiction because party failed to exhaust her administrative remedies before the SEC).

Gupta concedes that he has not exhausted his administrative remedies. Instead, he argues that he should be excused from challenging the OIP administratively. But the limited exceptions to the doctrine recognized by the Second Circuit—where (1) the claim is collateral, (2) "exhaustion would be futile," or (3) "requiring exhaustion would result in irreparable harm"—are not available to Gupta, as "[w]here administrative remedies are statutory . . . exhaustion of remedies is mandatory, and the exceptions do not apply." *Saint Regis Mohawk Tribe*, 451 F.3d at 50 (citations and quotations omitted).

Even if the exceptions applied here, Gupta cannot show that he meets any of them. First, Gupta has not shown that his claim is collateral. He is not challenging the validity of Section 929P; he is only challenging its potential application to him. His argument to this Court that Section 929P should not be applied is presumably identical to the argument that he would advance before the SEC. The issue is therefore not collateral. *See, e.g., Pavano v. Shalala*, 95 F.3d at 147 (finding that district court should not have waived exhaustion requirement where, among other things, the issue raised by plaintiffs was not collateral to administrative action).

Second, Gupta has not shown that exhaustion would be futile. Gupta alleges that administrative review would be futile (Complaint ¶ 19), complaining that the Commission appears biased against him (Complaint ¶¶ 19-22). Courts have repeatedly refused to excuse the exhaustion requirement merely because a party claims it would be futile to do so because an agency is purportedly biased. *See, e.g., Touche Ross*, 609 F.2d at 575 (and cases cited therein). Finding futility here is unwarranted because the SEC has never issued any decision on the retroactive application of Section 929P of Dodd-Frank. In addition, Gupta provides no reason to believe that the SEC will disregard any meritorious due process arguments.

Third, Gupta has not shown that requiring exhaustion would result in irreparable harm. Gupta claims that he will be forced to spend time and money in the administrative proceeding and that his reputation will be damaged. Complaint ¶ 18. As noted above, generally, the "expense and annoyance" involved in litigation do not constitute irreparable harm. *SoCal*, 449 U.S. at 244. Similarly, Gupta's unfounded contention that the administrative proceeding, as opposed to the district court action, is harming his reputation is meritless. Such a claim, even if true, is not sufficient to support an injunction. *First Jersey Secur., Inc. v. SEC*, 553 F. Supp. 205, 208-09 (D.N.J. 1982).

IV. Gupta Is Not Entitled to Injunctive Relief Because His Claim Fails as a Matter of Law.

Gupta's claim seeking to permanently "enjoin[] the Commission from pursuing its order against [him] administratively and from otherwise violating his due process rights" should be dismissed pursuant to Fed. R. Civ. P. 12(b)(6) because it fails to state a claim upon which relief may be granted. "To obtain a permanent injunction, a plaintiff must succeed on the merits and show the absence of an adequate remedy at law and irreparable harm if the relief is not granted."

Roach v. Morse, 440 F.3d 53, 56 (2d Cir. 2006). Here, Gupta has not even alleged facts which, if established, would satisfy the basic and necessary elements of a claim for injunctive relief.[13]

First, Gupta is not entitled to injunctive relief because he has an adequate remedy at law. As discussed above, he can raise his due process arguments and any concerns he has about the application of Dodd-Frank in the administrative proceeding and then in any appeal. The Second Circuit has long held that equitable relief is not available when an adequate remedy at law exists. *SCM Corp. v. Xerox Corp.*, 507 F.2d 358, 363 (2d Cir. 1974).

Second, Gupta has not alleged facts demonstrating irreparable harm. The only injury alleged by Gupta is that he will be "forced to expend time and money in an administrative appeal process—while his public image is being tarnished." Complaint ¶ 18. It is well established that the "expense and annoyance" of litigation does not constitute irreparable injury. *SoCal*, 449 U.S. at 244. Similarly, adverse publicity "may be an unfortunate consequence of an enforcement action, but such publicity does not warrant the issuance of an injunction against such proceedings." *First Jersey*, 553 F. Supp. at 212. Thus, Gupta's inability to identify any "imminent and irreparable harm further supports the dismissal of [his] complaint seeking permanent injunctive relief." *McMillan v. N.Y. State Bd. of Elections*, 2010 U.S. Dist. LEXIS 109894, at *43 (E.D.N.Y. Oct. 15, 2010).

[13] This motion to dismiss under Rule 12(b)(6) does not address whether any of Gupta's substantive allegations regarding retroactivity or due process fail to state a claim. As Gupta could raise these claims in the administrative proceeding where the Commission is the ultimate decision maker, the brief does not take a position those potential claims. The fact that this memorandum does not address these claims should not be viewed by the Court as having any bearing on the meritoriousness of those claims.

CONCLUSION

For the reasons stated, the SEC respectfully requests that the Court dismiss the Complaint.

Dated: April 1, 2011
Washington, D.C.

Respectfully submitted,

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