

APPEALS COURT DENIES CHALLENGE TO SEC RULE REQUIRING SETTTLING PARTIES NOT TO DENY LIABILITY

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The SEC's longstanding practice of requiring settling parties not to deny the charges against them, denounced as the "gag rule" by critics, recently withstood another legal challenge.

In *Powell v. Securities and Exchange Commission*, No. 24-1899 (August 6, 2025), the U.S. Court of Appeals for the Ninth Circuit rejected a challenge to the SEC's practice of settling cases only if the defendant agrees not to deny the SEC's allegations against them. As a result of that practice, SEC settlements typically provide that defendants may say they "neither admit nor deny" the allegations.

Along with a similar outcome in the Second Circuit in 2021, the Ninth Circuit decision leaves the SEC free to continue insisting on such language in its settlements. But the Ninth Circuit made clear it was only rejecting a "facial" challenge to the constitutionality of the rule, leaving future litigants free to argue that it was applied unconstitutionally in a particular case.

At the heart of the challenge, originally brought by a group named the New Civil Liberties Alliance ("NCLA"), is the argument that the rule violates defendants' speech rights under the First Amendment by preventing them from publicly criticizing the SEC. The court, however, noted that under U.S. law, "voluntary relinquishment of constitutional rights is permissible, so long as appropriate safeguards are attached."

The court also noted that defendants in SEC actions are free not to settle, and to go to trial or administrative hearing and defend against the charges. That a large percentage of SEC actions results in settlements does not mean that defendants' decisions, such as accepting a bar on denying the allegations as part of settlement terms, are involuntary.

In its decision, the Ninth Circuit also relied on the limited remedy available to the SEC in the event a settling party made public statements in violation of the prohibition on denying allegations. Its remedy is to go back to court, and ask that the case be reopened, without a guarantee that a judge would do so.

The SEC adopted the rule in question in 1972. It stated then that it “hereby announces its policy not to permit a defendant or respondent to consent to a judgment or order that imposes a sanction while denying the allegations in the complaint or order for proceedings. In this regard, the Commission believes that a refusal to admit the allegations is equivalent to a denial, unless the defendant or respondent states that he neither admits nor denies the allegations.” 17 C.F.R. § 202.5(e). While the SEC has in certain cases insisted on an admission of allegations as a condition of settlement, the “neither admit nor deny” language is most common in SEC settlements, and is also a common feature in settlements of charges by the Financial Industry Regulatory Authority (“FINRA”) as well.

The NCLA organization initially submitted its request in 2018 for the SEC to modify its rule. NCLA then modified its request in 2023, adding certain individuals who had settled with the SEC as petitioners. The SEC denied the requested modification in 2024, and 12 petitioners then challenged the SEC’s decision in the Ninth Circuit. The Ninth Circuit held that at least one of these individual petitioners, who had previously settled an SEC action and agreed to a settlement that prevented him from denying the allegations, had standing to challenge the SEC’s refusal to amend.

From the SEC’s perspective, the Ninth Circuit decision is a meaningful victory, in that it leaves standing its approach to settlement. But parties seeking to challenge the rule took some comfort in the court’s description of its decision as narrow, resolving only a facial challenge – meaning they may be free in particular cases to contend that their assent to the SEC’s language preventing them from denying the allegations was not voluntary. How courts respond to such challenges will have an important effect on SEC settlement practices in the future.

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