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**Client Alert** | Securities Litigation  
& Enforcement and Investment Management



## D.C. Circuit Ruling: Continued Challenges to FINRA Authority

The U.S. Court of Appeals for the D.C. Circuit has held that the Financial Industry Regulatory Authority (FINRA) may not expel a member firm, Alpine Securities Corp., in an expedited proceeding before Alpine obtained full review by the U.S. Securities and Exchange Commission (SEC) of the merits of any expulsion decision or before the period for Alpine to seek such review had elapsed.<sup>1</sup> In its November 22 decision in [Alpine Securities v. FINRA](#), the court granted Alpine's request for a preliminary injunction because Alpine demonstrated that it was likely to succeed on the merits of its challenge to FINRA's expulsion order pursuant to the private nondelegation doctrine and that it faced irreparable harm if expelled from FINRA.

### Key Takeaway

While a relatively narrow holding related solely to expedited disciplinary decisions seeking expulsions, the court's opinion foreshadows possibly broader constitutional challenges to FINRA's enforcement and other non-governmental disciplinary programs.

### Procedural Background

As required by the Securities Exchange Act of 1934, broker-dealer Alpine is a member of the self-regulatory organization FINRA and therefore subject to enforcement proceedings before the FINRA Office of Hearing Officers for violations of FINRA rules.

In March 2022, a [panel of FINRA hearing officers](#) found that Alpine violated certain FINRA rules, including those that prohibit charging unreasonable fees and misappropriating client assets.<sup>2</sup> The panel expelled Alpine from FINRA membership and ordered that it cease and desist from unlawful conduct and pay restitution and administrative costs. Alpine appealed to FINRA's internal appellate body, the National Adjudicatory Council. Although that appeal automatically stayed the expulsion order, it did not stay the cease-and-desist order, which required Alpine to stop charging unfair prices and commissions. Alpine could have appealed the cease-and-desist

<sup>1</sup> *Alpine Securities v. FINRA*, No. 23-5129, 2024 WL 4863140 (D.C. Cir. November 22, 2024).

<sup>2</sup> *Department of Enforcement v. Alpine Securities*, Disciplinary Proceeding No. 2019061232601 (FINRA Office of Hearing Officers March 22, 2022).

order to the SEC but chose not to, so that order went into and remained in effect as of the date of the D.C. Circuit's decision.

Alpine and its affiliate sued FINRA in the U.S. District Court for the Middle District of Florida, challenging FINRA's constitutionality pursuant to the private nondelegation doctrine and the Appointments Clause, as well as the First, Fifth and Seventh amendments.<sup>3</sup> In May 2023, the case was transferred to the U.S. District Court for the District of Columbia, where it is currently stayed.

While Alpine's lawsuit was pending, FINRA's Department of Enforcement opened an investigation into Alpine's alleged violations of the cease-and-desist order, specifically regarding certain fees that Alpine charged to its customers. Enforcement staff instituted an expedited disciplinary proceeding against Alpine and sought to immediately expel Alpine from FINRA membership.

Alpine sought a preliminary injunction against FINRA's expedited proceeding in district court, which was denied. The D.C. Circuit granted Alpine's request for an emergency injunction pending its appeal. On November 22, the D.C. Circuit reversed the lower court's decision.

### **A Narrow but Noteworthy Limitation on FINRA's Authority**

Because this was a proceeding concerning a preliminary injunction, the court did not reach the merits of Alpine's underlying case. Nevertheless, the D.C. Circuit's opinion is significant. In determining that Alpine was entitled to a preliminary injunction, the D.C. Circuit found that Alpine was likely to prevail on the merits of its private nondelegation claim as it related to FINRA's expedited hearing process.

The private nondelegation doctrine prevents private entities from exercising executive power in the absence of governmental supervision. As the court explained, for a delegation of governmental authority to a private organization to be lawful, the private entity must act only "as an aid to an accountable government agency that retains the ultimate authority to approve, disapprove, or modify the private entity's actions and decisions on delegated matters."<sup>4</sup>

FINRA, as a private organization tasked with regulating member firms under not only its own rules but the federal securities laws, is subject to SEC supervision. With respect to discipline administered by FINRA, the SEC reviews de novo any appeals of final decisions to impose sanctions and has the authority to approve, disapprove or modify any actions taken by FINRA. However, this process does not apply to expedited proceedings to expel members from FINRA, such as the one brought against Alpine.

The court noted that expulsion orders occurring under expedited proceedings take effect immediately — without any opportunity for review by the SEC. The consequences of an expulsion are extreme, as they effectively put the member firm out of business. Even if the SEC were to later review the expulsion decision, the damage to the member firm already would have been done.

Although there is a process by which the SEC may stay the effectiveness of an expulsion order issued after an expedited proceeding, the court did not find this sufficient to satisfy the

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<sup>3</sup> *Scottsdale Capital Advisors v. FINRA*, No. 1:23cv1506 (D.D.C. filed October 12, 2022).

<sup>4</sup> *Supra* n.1 at 17 (internal quotations and citations omitted).

requirements of the private nondelegation doctrine. First, the court noted, the stay is not automatic. Second, whether the SEC grants a stay is not a decision on the merits. Thus, Alpine was barred by FINRA from trading under the federal securities laws without any possibility for SEC review of FINRA's decision on the merits.

For the foregoing reasons, the court found Alpine's expulsion pursuant to expedited proceedings to be a violation of the private nondelegation doctrine. The court was careful to state that this was a limited opinion for four reasons: first, the issue came up for review on a motion for a preliminary injunction; second, the opinion was limited to expulsion orders issued in expedited proceedings; third, the opinion did not address either FINRA or the SEC's ability to alter its own procedures for stays, going forward; and fourth, the opinion does not question the constitutionality of enforcing any FINRA sanctions after the SEC has affirmed them.

### **Judge Walker's Opinion Suggests More Significant Checks on FINRA Authority**

As noted at the outset, Alpine's case on the merits challenging the constitutionality of FINRA is still pending in the U.S. District Court for the District of Columbia. The D.C. Circuit's opinion on the preliminary injunction does not reach the merits of Alpine's underlying case. Despite that, an opinion by Judge Justin Walker — concurring in part and dissenting in part — offered a view more broadly of the constitutionality of FINRA's authority as a private self-regulatory organization. First, Walker stated if FINRA is a private entity, it is likely in violation of the private nondelegation doctrine because of the vast array of powers that FINRA may exercise with no SEC oversight whatsoever, including, for example, opening an investigation; negotiating settlements; and demanding to inspect books, records and accounts. Per Walker, it is insufficient for there to be SEC review of the final decision/sanction reached in a disciplinary proceeding because of the "vast array of powers that FINRA exercises before the matter even reaches the SEC."<sup>5</sup>

Second, if FINRA is a "governmental entity," Walker observed that FINRA would be in violation of the Appointments Clause, which requires executive officers to be properly appointed under the Constitution and removable by the president. Walker further noted that "FINRA's hearing officers are indistinguishable from the administrative law judges in *Lucia* and the special trial judges in *Freytag*"<sup>6</sup> — two cases in which the U.S. Supreme Court previously found violations of the Appointments Clause at the SEC and Internal Revenue Service, respectively.

### **Takeaway for Broker-Dealers**

Broker-dealers that are currently under investigation by or in disciplinary proceedings before FINRA should take careful note of this case and the accompanying case pending before the U.S. District Court for the District of Columbia. Although the FINRA Department of Enforcement, Office of Hearing Officers and National Adjudicatory Council exercise broad authority, their judgments and determinations are subject to review by both the SEC and the federal courts.

The change in administration and, in particular, the leadership at the SEC, combined with the increasing skepticism of the courts toward administrative tribunals and certain administrative decision-making suggests that there may be more changes to come. In the meantime, where

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<sup>5</sup> *Id.* at 16 (Walker, J., concurring in the judgment and dissenting in part).

<sup>6</sup> *Id.* at 19 (citing *Lucia v. SEC*, 585 U.S. 237 (2018), and *Freytag v. Commissioner*, 501 U.S. 868 (1991)).

once it may have seemed farfetched to bring constitutional challenges to FINRA's authority, these challenges should be considered when involved in a contentious matter with FINRA.

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