SEC Senior Enforcers Speak on SEC Hot Topics

by Larry P. Ellsworth, Thomas C. Newkirk and Elaine Wolff

The recently created senior management team who works with the Director of Enforcement of the Securities and Exchange Commission ("SEC") presented its views of new developments and hot topics facing the Division of Enforcement during a District of Columbia Bar Association panel discussion on October 22, 2008, held at the Washington, DC offices of Jenner & Block LLP. This Client Advisory highlights the significant matters discussed by Chief Counsel, Joan McKown, and the two new Deputy Directors, Scott Friestad and George Curtis, at the panel discussion moderated by Jenner & Block Partner Larry Ellsworth.

The Enforcement management team pointed out that the deputy/chief counsel management structure has grown and evolved in response to the growth in size and complexity of investigations, globalization of cases, advances in technology and the Division's additional responsibilities such as managing the distribution of increasingly large collections to investors, as well as the size of the staff.

Enforcement Priorities

The SEC's enforcement priorities are largely reflected in its existing working groups on auction rate securities, subprime issues, hedge funds and insider trading, stock option backdating, and municipal securities, which are designed to deal with issues in a coordinated fashion.

- The subprime working group involves 150 staff nationwide and includes credit market and other credit issues. The focus is on misrepresentation, valuation and marketing issues.
- Auction rate securities cases have required significant resources. Most companies are settling these actions for business reasons, but there will be actions against individuals which may result in litigation.
- The Division is also working to finish the approximately 80 remaining (out of 100) stock option backdating investigations by the end of the calendar year, although some of these cases have evolved into cases involving other issues. These 80 cases include the cases already brought involving about 25 issuers.
- Financial fraud and insider trading remain core program areas. While there may be fewer large financial fraud cases now than a few years ago, these types of cases normally increase in down markets.

- New priorities include securities marketing issues, the interrelationship between various classes of securities, short selling by hedge funds, broker dealers and institutional investors as well as trading in credit default swaps.
- Scott Friestad says that we should expect to see a number of major new Foreign Corrupt Practices Act cases. In the last two years the Commission has brought close to 30 FCPA cases, which is more than all previous FCPA cases combined. While a majority of the FCPA investigations involve violations that were self-reported, a significant number of the present investigations were generated by other leads.

Tips for Informal Meetings with Staff

Although it may appear self-evident, the Enforcement management team emphasized that counsel meeting with senior SEC staff ought to focus on addressing staff concerns, responding to questions, and limiting arguments to the two to three best arguments with which the staff may not have previously agreed.

Catalyst for Making Enforcement Manual Public

This month, for the first time, the SEC published a Division of Enforcement Manual ("Manual") that is available to the public on the SEC website at http://sec.gov/divisions/enforce/enforcementmanual.pdf. The Enforcement management team stressed that the Manual does not reflect new policies, but collects in one place and reduces to writing policies that were in place but not easily accessible even within the SEC. These policies evolve over time taking into account new experience.

Deputy Director Involvement in Process of Authorizing Investigations

In response to inquiries regarding delays in SEC investigations, George Curtis said in regard to the relatively new process for opening investigations, that the Deputies strive to turn around MUI (matters under investigation) requests within 24 hours. He said Deputy involvement at this initial stage facilitates finding the correct venue and coordination of similar investigations in different offices. According to Joan McKown, when the staff has looked into the causes of significant delays, they found the delay to generally occur at the settlement stage.

Section 21(a) Reports

Joan McKown says that the recent report issued by the Commission pursuant to Section 21(a) resolving its investigation of the Retirement Systems of Alabama involving control person liability and insider trading compliance programs, does not reflect any new initiative to use more such reports. She explained that the Commission generally will exercise its authority to publish a report finding a violation pursuant to Section 21(a) without seeking a remedy only when there is a significant, new message to be delivered of which people are generally unaware. She agreed with the moderator, Larry Ellsworth, that over the years the Commission has averaged only about two such reports every three years.

Section 21(a) (1) Orders

Instead of following its normal practice of issuing individual subpoenas for information, the Commission recently issued a broad order to numerous hedge funds, broker-dealers and institutional investors for written sworn statements, similar to interrogatories in litigation. The order concerns their positions in credit swaps and certain other significant trading activities. The Enforcement management team explained that, since the Commission issues these orders, the staff has less discretion than on a subpoena to limit the scope of production requests.

Closing Process and Termination Letters

Stressing that the process to close an investigation has not changed, Joan McKown pointed out that she reviews all closings-without-action and that a Deputy Director must authorize the closing of an investigation. She indicated that a person involved in the investigation who requests a termination letter, is named in a formal order, or receives a Wells Notice, should in the normal course receive a termination letter. This does not mean that there is an "entitlement" to a termination letter. However, the senior staff would need to approve a decision not to send a letter, which may occur when, for example, the staff is continuing to look at other individuals involved in the investigation.

For more information, please contact the following Jenner & Block attorneys:

Larry P. Ellsworth
Partner
Tel: 202 639-6032
Email: lellsworth@jenner.com

Thomas C. Newkirk
Partner
Tel: 202 639-6099
Email: tnewkirk@jenner.com

Elaine Wolff
Partner
Tel: 202 637-6389
Email: ewolff@jenner.com