

[Securities Regulation Daily Wrap Up, TOP STORY—More than numbers: Clayton, Avakian tout enforcement program successes, \(Sept. 21, 2020\)](#)

Securities Regulation Daily Wrap Up

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Current and former enforcement directors assured that statistics related to the Division's efforts do not tell the whole story, especially given the lack of resources afforded to the Commission.

The University of Pennsylvania's Institute for Law and Economics welcome backed its law school alumnus, SEC Chairman Jay Clayton, for a discussion on the Commission's enforcement program. Praising the SEC's "nimble enforcement" of the nation's securities laws, Clayton highlighted the successes of the Enforcement Division under his tenure and warned against drawing too many conclusions from statistics about the enforcement program, such as number of cases and monetary awards. Clayton was joined by Enforcement Director Stephanie Avakian and four former directors, including Avakian's former co-director Steve Peikin.

Measuring success. Clayton [said](#) that the Division's focus has been shaped by three principles: (1) getting harmed retail investors their money back promptly; (2) pursuing matters that will have a lasting and deterring impact; and (3) instilling confidence in the integrity and fairness of markets. Clayton highlighted the work of the Retail Strategy Task Force, citing in particular its work on protecting retail investors from unnecessary fees and expenses. As an example, he pointed out the Commission's [Share Class Selection Disclosure](#) initiative, which encouraged investment advisers to self-report violations of the Advisers Act resulting from undisclosed conflicts of interest and resulted in \$130 million being returned to investors.

Clayton also praised the Enforcement Division's work in the area of ICOs, describing ICO activity of late 2016 and 2017 "a mess." The SEC responded to the flurry of ICO activity quickly, including issuing an investigative report confirming the application of the federal securities laws to these types of offerings, the creation of the SEC's Cyber Unit, and bringing a series of actions against the unregistered sales or fraudulent offerings of these tokens, Clayton said.

The Division's "nimble nature" was also on display in its response to the COVID-19 crisis, according to Clayton. In addition to suspending trading in the securities of three dozen companies related to their statements about COVID issues such as personal protective equipment and effective COVID-19 tests, the Enforcement Division followed up on some of these suspensions with fraud actions against issuers and individuals.

Clayton remarked that the Enforcement Division's work is not readily apparent in traditional metrics such as number of cases and total monetary relief. "Ironically," Clayton mused, "the faster and more effectively we act, the lower some of these numbers should be." That is why he is most interested in the combination of money returned to investors (harm remedied) and money saved by investors (harm prevented).

Echoing Clayton's remarks, Avakian [said](#) that the numbers boasted by the Enforcement Division do not adequately convey the quality, nature, and effectiveness of the SEC's efforts. The Division has focused on the most serious violations, obtaining meaningful punishments that deter unlawful conduct, recouping ill-gotten gains to return to investors, and incapacitating wrongdoers, Avakian advised.

Avakian highlighted Enforcement's focus on financial fraud and issuer disclosure, including enforcement actions brought against Theranos, Hertz, Wells Fargo, Walgreens, Facebook, Nissan, and Volkswagen, some of which also included charges against company executives. The SEC has also brought important actions against registrants who have negatively impacted market integrity, Avakian said. In this area, she cited actions against 15 financial institutions, including JP Morgan Chase, Citibank, and Merrill Lynch for improper conduct

in connection with the pre-release of American Depository Receipts, which resulted in over \$430 million in disgorgement and penalties.

Also in the sphere of market integrity, Avakian cited enforcement actions brought against firms that sold unsuitable products to retail investors, complex market structure cases involving order handling, and enforcement actions against exchanges for regulatory failures in connection with disruptive market events and failures related to financial risk management and IT security. Other areas of focus by the Enforcement Division include insider trading, the Foreign Corrupt Practices Act, Ponzi schemes and other offering frauds, and ICOs.

Avakian also addressed recent challenges presented to the SEC's enforcement program, including Supreme Court decisions, the 35-day government shutdown in 2019, and a the COVID-19 pandemic. Regarding the Supreme Court's decisions, Avakian noted that the Supreme Court's 2017 [Lucia](#) opinion, which held that SEC ALJs were Article II officers, resulted in the Commission ordering that respondents in pending ALJ cases or Commission appeals be provided with the opportunity for a new hearing before a different ALJ. According to Avakian, the Enforcement Division's investigators and litigators had to revisit 200 remanded cases, some of which were more than a decade old, which required significant effort and resource allocation.

The SEC was also dealt a blow by the Supreme Court's [Kokesh](#) decision, which held that the federal five-year statute of limitations applies to SEC disgorgement orders. Avakian said that the Commission estimated that it had to forgo approximately \$1.1 billion in disgorgement following [Kokesh](#) and had to reevaluate how it addressed disgorgement in its active investigations and litigation. She pointed out, however, that despite collateral attacks on the Commission's ability to seek disgorgement in the aftermath of [Kokesh](#), not a single court ruled against the SEC, including the Supreme Court in [SEC v. Liu](#) earlier this year. While the Court in [Liu](#) imposed some limitations on the SEC's disgorgement authority, it held that disgorgement is available to the SEC in its enforcement actions, Avakian said.

Former directors chime in. One question posed to the panelists inquired how to measure the deterrent affect of the Division's actions in the long term if the statistics do not paint the full story of enforcement. Clayton replied that deterrence is about people making decisions knowing that someone is watching. And while enforcement is a big part of it, deterrence also involves independent directors, outside counsel, compliance officers, or some combination, he said. Avakian added that individual accountability is one of the most critical things the Commission can do to effect deterrence, noting that 70 percent of the time, the SEC's enforcement program seeks to deter wrongdoing by holding individuals accountable.

Former Enforcement Director Linda Chatman Thomsen, now at Davis Polk & Wardwell LLP, remarked that measuring deterrence has been extraordinarily difficult, and Avakian agreed, especially when it comes to measuring what the Commission does not know and what drives people. The most we can do is continue to bring meaningful actions with meaningful remedies and hope that it makes a difference, she said.

Steve Peikin, who left his position as co-director of the Division of Enforcement in August, said that bringing actions close in time to when the conduct occurred sends the strongest message. He pointed to the SEC's enforcement action against Tesla and Elon Musk, which is notable not just for its notoriety, but also for the speed with which the Commission was able to act, Peiken said. Bringing actions three to five years after the misconduct just doesn't have the same deterrent effect, he advised.

Peikin also offered his thoughts on the Division's recent statistics. According to Peikin, it is "silly" to judge the Commission's vigor in pursuing cases by looking at a pile of cases that were filed in a particular period because some cases could have involved years of work to unravel. Bill McLucas, who headed the Enforcement Division for eight years and is now the chair of WilmerHale's securities department, agreed that the numbers do not tell the whole story about the enforcement program and whether it has been effective. He quipped that he always hated September (the end of the fiscal year) because everyone was focused on the numbers and the Division would be lauded or criticized depending on what the numbers said, including battling with members of the press.

Former Enforcement Director Steve Cutler, now at Simpson, Thacher & Bartlett, remarked that U.S. Attorneys are not subject to similar scrutiny of numbers compared to the SEC. Measuring success through numerical

metrics does not do justice to the SEC's efforts, Cutler said. In particular, relying on the number of cases brought is not a useful metric, he added.

The former directors also discussed challenges regarding resource allocation at the SEC. For every matter the Division is working on, it's not working on another, Cutler said. Cutler asked Peikin how the Enforcement Division during his tenure dealt with scarce resources and a hiring freeze. Peikin said one area that did not receive as much attention involved "regulator cases" against registrants, such as referrals from examinations, where a small amount of money had been lost and repaid. In "fatter times," the Division may have brought those cases, but given the SEC's resources, the Division chose to focus on other areas, including cases involving retail investors, Peikin said.

Thomsen noted that the SEC has always been understaffed with too much to do, citing in particular her experience in the post-9/11, post-Enron era when the Sarbanes-Oxley Act required Commission action on a "pile of" rulemaking requirements. Echoing Cutler's earlier remarks, Thomsen added that the SEC has been subject to criticism in the way that other government agencies are not.

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