Despite Unprecedented Challenges, SEC's Division of Enforcement 2020 Annual Report Presents Healthy Enforcement Results

November 3, 2020

On November 2, 2020, the U.S. Securities and Exchange Commission's (the "SEC" or "Commission") Division of Enforcement (the "Division") released its 2020 Annual Report (the "Report"), which details the Division's activities and results for the period October 1, 2019 to September 30, 2020. The Report highlights the substantial impact of the COVID-19 pandemic on the Division's activities, including the challenges of moving investigations forward while working remotely and the need to divert significant resources to protecting retail investors by investigating potential pandemic-related misconduct. While the Report notes that the COVID-19 pandemic reduced the number of cases the Commission filed—405 standalone cases in 2020 compared to 526 in 2019—by contrast, the remedies obtained by the Commission set a new record in 2020 at $4.68 billion ($1.09 billion in penalties and $3.589 billion in disgorgement). In addition, 2020 was a banner year for the SEC's Whistleblower Program, with a record total of $175 million in awards issued to 39 individuals, accounting for roughly 37% of the total number of awards over the life of the program.

The Division's Director, Stephanie Avakian, described FY 2020 as "the most challenging year in recent memory" but noted that despite the challenges, the Division "demonstrated its agility" in quickly moving to address enforcement-related issues arising from the COVID-19 crisis. In particular, the report highlights the Division's efforts to adapt to the pandemic by finding innovative ways to conduct testimony and depositions and hold Wells meetings remotely. The Report also notes that the Division opened more than 150 inquiries and investigations related to COVID-19 during FY 2020 and brought several COVID-related fraud actions. In addition to COVID-19, the Report highlights Division cases and initiatives in the following areas: (1) detecting, remedying, and punishing misconduct by issuers and registrants; (2) holding individuals accountable; and (3) protecting retail investors. Interestingly, this year's Report did not focus as heavily as it has in the past on digital assets and the Division's efforts to address cyber threats, which included the creation of a Cyber Unit three years ago.

FY 2020 by the Numbers

The Division brought 715 enforcement actions in FY 2020—a decrease of 17% from last year. This 715 total includes 405 standalone enforcement actions, 180 follow-on administrative proceedings, and 130 actions to deregister public companies delinquent on their SEC filings. 72% of the standalone actions involved charges against one or more individuals, which is similar to past years and reflects the Division's continued focus on individual accountability. Additionally, 40% of the standalone actions were filed in whole or in part as litigated actions in FY 2020, compared to 30% in FY 2019.

Three enforcement areas drove the majority of the SEC's standalone cases:

- Securities offerings (32% of the total);
- Investment advisory and investment company issues (21%); and
- Issuer reporting/accounting and auditing matters (15%).

Notably, offering fraud actions made up approximately one-third of the standalone actions brought during FY 2020, representing an increase over each of the prior years during the Trump administration. By contrast, the percentage of cases involving investment advisory and investment company issues dropped to historically normal levels compared to FY 2019, which included a significant number of standalone actions resulting from the Division's self-reporting Share Class Selection Disclosure Initiative ("SCSDI"). The percentage of standalone actions involving issuer reporting, disclosure, and auditor issues also remained relatively consistent year over year.

The SEC also brought cases related to broker-dealers (10%), insider trading (8%), market manipulation (5%), Public Finance abuse (3%), and the FCPA (2%). The number of insider trading cases remained fairly consistent year over year, increasing to 33 from 30 in FY 2019, although this figure was substantially higher in FY 2018 (51) and FY 2017 (41).

Total monetary relief ordered, including disgorgement and penalties, increased from FY 2019 by $330 million (approximately 8%) to $4.68 billion, a new record high for the Division that was primarily driven by the 10% increase in disgorgement ordered during FY 2020. This increase in disgorgement can be attributed to several key cases, including the Commission's emergency action against Telegram Group Inc.,[1] which agreed to return more than $1.2 billion to resolve charges that it engaged in an unregistered

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1 Press Release, Telegram to Return $1.2 Billion to Investors and Pay $18.5 Million Penalty to Settle SEC Charges (June 26, 2020), https://www.sec.gov/news/press-release/2020-146.

offering of digital tokens, as well as a number of FCPA settlements, such as the December 2019 action against Telefonaktiebolaget LM Ericsson,[2] which agreed to pay more than $539 million in disgorgement and prejudgment interest.

The Commission returned $602 million to harmed investors in FY 2020, which represents a 50% decrease from FY 2019. However, this year's figure is roughly consistent year over year considering that half of the FY 2019 distributions stemmed from three Fair Funds and one disgorgement fund resulting from cases that were resolved in prior years.

The Report also highlights nonmonetary relief obtained in enforcement actions, including undertakings, bars and suspensions, and asset freezes. During FY 2020, enforcement actions resulted in 477 bars and suspensions for individuals and trading suspensions for 196 issuers. The Division also obtained 24 court-ordered asset freezes—a tool the Commission uses to prevent alleged wrongdoers from moving assets that could potentially be subject to disgorgement and returned to investors. All of these figures represented decreases from FY 2019.

Focus on Financial Fraud and Issuer Disclosure

The Report noted the Commission's continued focus on identifying and investigating potential securities laws violations involving the financial reporting process, which has traditionally been an area of focus for the Division. In particular, the Report highlighted eight enforcement actions involving fraudulent accounting practices, five of which focused on improper revenue recognition. The Report also highlighted other cases involving revenue recognition issues—for example, actions against Diageo plc[3] and HP Inc.[4]—that did not include accounting violations, but nonetheless resulted in disclosure violations due to the companies' failure to disclose the impact of the accounting practices at issue. Additionally, as it has in recent years, the Report highlighted cases involving inaccurate and misleading use of non-GAAP metrics and key performance indicators.

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2 Press Release, SEC Charges Multinational Telecommunications Company With FCPA Violations (Dec. 6, 2019), https://www.sec.gov/news/press-release/2019-254.

3 *In the Matter of Diageo plc*, Exchange Act Release No. 88234 (Feb. 19, 2020), https://www.sec.gov/litigation/admin/2020/33-10756.pdf.

4 *In the Matter of HP Inc.*, Exchange Act Release No. 90060 (Sept. 30, 2020), https://www.sec.gov/litigation/admin/2020/33-10868.pdf.

Data Analytics

As part of its focus on pursuing financial fraud and issuer disclosure violations, the Division continues to focus on leveraging new technologies and data analytics to identify potential violations, which led to a new initiative that resulted in several enforcement actions during FY 2020. In September 2020, the Division announced its EPS (Earnings Per Share) Initiative, which utilizes risk-based data analytics to detect potential accounting and disclosure violations that might arise from improper earnings management practices.[5] The Division disclosed the initiative at the same time it announced settled actions with Interface, Inc.[6] and Fulton Financial Corporation[7] alleging improper accounting practices that allowed the companies to report quarterly EPS that met or exceeded analyst consensus estimates. Two days later, the Division announced a third settlement under the initiative against Hilton Worldwide Holdings, Inc.[8] for failing to sufficiently disclose perquisites provided to corporate executives. These cases underscore that data analytics, which has been a focus for the Division for a number of years, continues to be a critical tool employed by the SEC to detect potential securities law violations involving the financial reporting process.

Whistleblower Highlights

FY 2020 was also a record-breaking year for the SEC's whistleblower program, with the Commission issuing a total of $175 million in awards to 39 individuals—both records for the program. By comparison, during FY 2019 the SEC issued a total of $60 million to eight individuals. Given the lengthy investigative and subsequent award claim processes, whistleblower awards obviously represent awards for cases brought in prior years—sometimes several years earlier—but the increase suggests a more fluid process for approving awards. As the SEC saw a substantial increase of 40% in tips, complaints, and referrals ("TCRs") during FY 2020 and was able to triage 71% more TCRs than in prior years, the increasing level of activity under the SEC's whistleblower program is likely to continue. During the first month of FY 2021, the SEC has already issued approximately

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5 Press Release, SEC Charges Companies, Former Executives as Part of Risk-Based Initiative (Sept. 28, 2020), https://www.sec.gov/news/press-release/2020-226.

6 *In the Matter of Interface Inc. et al.*, Exchange Act Rel. No. 90018 (Sept. 28, 2020), https://www.sec.gov/litigation/admin/2020/33-10854.pdf.

7 *In the Matter of Fulton Financial Corporation*, Exchange Act Rel. No. 90017 (Sept. 28, 2020), https://www.sec.gov/litigation/admin/2020/34-90017.pdf.

8 *In the Matter of Hilton Worldwide Holdings, Inc.*, Exchange Act Rel. No. 90052 (Sept. 30, 2020), https://www.sec.gov/litigation/admin/2020/34-90052.pdf.

$125 million in whistleblower awards, including a $114 million award,[9] which is the largest award in the program's history.

Conclusion

Moving into FY 2021, we expect that the SEC's current level of enforcement activity will remain steady, if not increase, particularly depending on the results of a presidential election that could lead to an increased agency budget. Notably, new inquires and investigations during FY 2020 were up from the prior year—the Division opened 1,181 new inquiries and investigations in FY 2020, compared to 1,082 for FY 2019—which could be an indication that FY 2021 will be a busy year for the SEC, as the Division's staff that has now adjusted to working in a remote work environment turns its focus to delivering on its commitment to accelerate the pace of investigations. Additionally, the SEC's whistleblower program appears to be more active than ever as it continues to provide a steady stream of information leading to successful enforcement actions.

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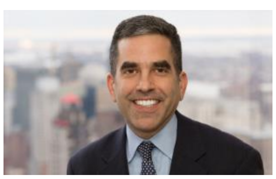

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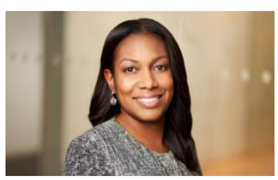

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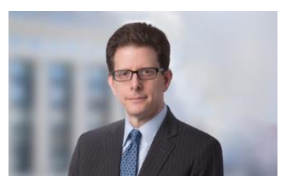

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9 Press Release, SEC Issues Record $114 Million Whistleblower Award (Oct. 22, 2020), https://www.sec.gov/news/press-release/2020-266.

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