

SEC's Division of Enforcement 2019 Annual Report Presents Strong Enforcement Results

November 7, 2019

On November 6, 2019, the U.S. Securities and Exchange Commission (the “SEC” or “Commission”) released its [2019 Annual Report](#) (the “Report”), which details the activities and results of the Division of Enforcement (the “Division”) for the period October 1, 2018 to September 30, 2019. The Report shows that the SEC’s enforcement numbers—which have trended lower during the Trump administration—held relatively steady in FY 2019. Eighteen percent of the 526 standalone actions brought by the Division in FY 2019 resulted from the self-reporting Share Class Selection Disclosure Initiative (“SCSDI”). That initiative, which the Division launched in 2018, offered registered investment advisers the opportunity to self-report allegedly inadequate disclosures related to the receipt of 12b-1 fees from mutual fund advisers based on clients’ investments. It resulted in \$135 million in total disgorgement from 95 standalone enforcement actions.¹

The Division’s Co-Directors, Stephanie Avakian and Steven Peikin, describe FY 2019 as a “very successful year” despite “significant headwinds,” which included the government’s 35-day shutdown and the Supreme Court’s 2017 decision in *Kokesh*,² which limited the time period for which the SEC could obtain disgorgement to five years, and 2018 decision in *Lucia*,³ which voided prior decisions by the SEC’s administrative law judges (“ALJs”) after determining that their appointments were constitutionally infirm. As they did in the FY 2018 Report, the Co-Directors de-emphasized the quantitative numbers and discussed the “qualitative factors, such as the nature, quality, and diversity of the SEC’s enforcement actions.” The Report highlights Division cases and initiatives relating to: (1) protection of main street investors; (2) detecting, remedying, and punishing misconduct by issuers and financial institutions; (3) holding individuals accountable; and (4) digital assets and distributed ledger technology cases.

¹ Press Release, SEC Orders an Additional 16 Self-Reporting Advisory Firms to Pay Nearly \$10 Million to Investors (Sept. 30, 2019), <https://www.sec.gov/news/press-release/2019-200>.

² Debevoise & Plimpton LLP, U.S. Supreme Court Holds SEC Disgorgement Is a Penalty Subject to a Five-Year Statute of Limitations (June 7, 2017), <https://www.debevoise.com/insights/publications/2017/06/us-supreme-court-holds-sec-disgorgement>.

³ Debevoise & Plimpton LLP, Insider Trading & Disclosure Update, *Lucia v. SEC*: Supreme Court Rejects Constitutionality of SEC ALJs (Oct. 2018), https://www.debevoise.com/-/media/files/insights/publications/2018/10/20181024_insider_trading_update_oct2018_v9.pdf.

FY 2019 by the Numbers

The Division filed 862 enforcement actions in FY 2019—the most in the Trump era and an increase of 5% from last year. This 862 total includes 526 standalone enforcement actions (95 of which were from the SCSDI), 210 follow-on administrative proceedings, and 126 actions to deregister public companies delinquent on their SEC filings.

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

- Investment adviser and investment companies (36% of the total) (which includes the SCSDI cases);
- Securities offerings (21%); and
- Issuer reporting/accounting and auditing matters (17%).

The SEC also brought cases related to broker-dealers (7%), insider trading (6%), market manipulation (6%), and the FCPA (3%). The number of insider trading cases was down from 51 in FY 2018 to 30 in FY 2019.

Total monetary relief ordered, including disgorgement and penalties, increased from FY 2018 by \$404 million (approximately 10%) to \$4.349 billion. As with last year's total, a single case drove a significant part of the \$3.248 billion total disgorgement imposed. This year, that case was a more than \$1 billion judgment in the U.S. District Court for the Southern District of Florida against the operators of the Woodbridge Ponzi scheme, which included over \$912 million in disgorgement against the company and its former CEO.⁴

In addition, the Commission returned \$1.197 billion to harmed investors in FY 2019, a 50% increase from FY 2018 that principally stemmed from three Fair Funds and one disgorgement fund resulting from cases resolved some years ago that distributed \$902 million to harmed investors.

The Report also highlights non-monetary relief obtained in enforcement actions, including undertakings, bars and suspensions, and asset freezes. During the year, enforcement actions resulted in 595 bars and suspensions for individuals (an increase over FY 2018) and trading suspensions for 271 issuers (a decrease from FY 2018). Also during FY 2019, the Division obtained 31 court-ordered asset freezes (an increase from 26 in FY 2018)—a tool the Commission uses to prevent alleged wrongdoers from

⁴ See Press Release, SEC, Court Orders \$1 Billion Judgment Against Operators of Woodbridge Ponzi Scheme Targeting Retail Investors (Jan. 28, 2019), <https://www.sec.gov/news/press-release/2019-3>.

moving assets that could potentially be subject to disgorgement and returned to investors.

The Report also highlights the SEC's use of undertakings to address specific risks, such as in the settled action with KPMG regarding its failures to have sufficient controls in place to prevent the misuse of PCAOB inspection information.⁵ Another example mentioned in the report was the settlement with the Options Clearing Corporation ("OCC") related to its failure to comply with certain statutes and rules applicable to registered clearing agencies deemed systemically important financial market utilities. The settlement required the OCC to retain an independent compliance auditor that would assess remediation and provide an annual compliance report to the OCC's Board, provide the OCC Board with all examination findings by the Commission's Office of Compliance Inspections and Examinations and OCC's responses, and file a rule change to create a Board-level regulatory committee separate from the audit committee.⁶

Focus on Retail and Digital Assets

The Report noted the Commission's continued focus on two areas: protecting main street investors and digital assets. With regard to the former, the Report highlights the success of the SCSDI, which had the "immediate benefit of more than \$135 million being ordered returned to harmed investors and the lasting benefit of improved disclosure."

In addition, the Report highlighted the work of the two-year-old Retail Strategy Task Force ("RSTF"), which has two objectives: (1) identify potential enforcement matters through the use of data analytics, and (2) collaborate with other divisions at the Commission on retail investor advocacy and outreach. Notably, however, the Report fails to attribute any specific cases or numbers to the work of the RSTF.

With regard to digital assets, the Division created the Cyber Unit two years ago to focus on cyber-related threats and enforcement matters. Among the cases highlighted in the Report were those brought against issuers of initial-coin offerings ("ICOs") for violations of the Securities Act of 1933, as well as against third parties who had participated in the same and were charged under various anti-touting, broker-dealer, and exchange registration provisions of the securities laws. Unlike in FY 2018 when the

⁵ See *In re KPMG LLP*, Exchange Act Release No. 86,118 (June 17, 2019), <https://www.sec.gov/litigation/admin/2019/34-86118.pdf>.

⁶ *In re OCC*, Exchange Act Release No. 86,871 (Sept. 4, 2019), <https://www.sec.gov/litigation/admin/2019/34-86871.pdf>.

Commission touted that it had brought 20 cases related to ICOs, no number breakdown was provided in the FY 2019 Report.

Resource Constraints

The Report notes that the Division is still feeling the effects of resource constraints coming off a two-year Commission-wide hiring freeze that was lifted on April 1, 2019. The Division added 15 new staff members in FY 2019, but the Division's staff numbers remain 9% lower than FY 2016, the last year of the Obama administration. The Division has authorization for additional hires but not the resources to replace all the staff lost since 2016. We expect the resource constraints to continue to depress enforcement numbers in the coming fiscal year.

Current and Future Investigations

The Report discusses “continuing areas of focus” of note for individuals and entities subject to SEC investigation. First, the Report notes the Division is focused on accelerating the pace of its investigations. The Commission's Inspector General has repeatedly, and as recently as last month, criticized the Division for its slow pace of investigation, which has failed to meet the target of 20 months from the opening of a matter to commencing an enforcement action.⁷ In FY 2019, the Report notes that the average matter length was approximately 24 months but said the Division is “taking steps to accelerate the pace of these investigations.”

Toward that goal, the Report also highlights the importance of cooperation by individuals and companies under investigation by the SEC. The Report uses the September settlement with PPG as an example; there, the Commission concluded its enforcement action 17 months after opening the matter and notably settled with PPG for no penalty despite a fraud finding related to misstatements in the company's filings.⁸ The PPG order attributes the lack of penalty to extensive cooperation provided by PPG, including self-reporting, implementation of immediate remedial measures, and ongoing cooperation with Commission staff during the investigation.

⁷ See Memorandum, SEC, Office of Inspector General, The Inspector General's Statement on the SEC's Management and Performance Challenges (Oct. 2019), <https://www.sec.gov/files/Inspector-Generals-Statement-on-the-SECs-Mgt-and-Performance-Challenges-Oct-2019.pdf>.

⁸ *In re PPG Industries, Inc.*, Securities Act Release No. 10,701 (Sept. 26, 2019), <https://www.sec.gov/litigation/admin/2019/33-10701.pdf>.

The Report also discusses the ongoing Division focus on holding individuals accountable for wrongdoing, which the Commission sees as achieving “multiple goals, including specific and general deterrence and, where injunctive and other non-monetary remedies are imposed, protection of markets and investors from future misconduct by those same bad actors.” Excluding the SCSDI cases, 69% of the standalone cases in FY 2019 had charges against one or more individuals.

Conclusion

Although the Report offers little in terms of statistics from which to extrapolate future enforcement numbers, we expect the enforcement levels of the past couple of years to continue into the Commission’s FY 2020. Although the Division has added new staff, the increased headcount is relatively modest and unlikely to significantly alter the total enforcement numbers. The Report does note the continued success of its whistleblower program, which will be the subject of a separate Commission report later this month and which has provided a steady stream of information that has led to enforcement actions for the Commission.

In addition, developments at the Supreme Court and in Congress stemming from the 2017 *Kokesh* decision may affect the SEC’s ability to obtain disgorgement from subjects of enforcement actions. Earlier this week, in *Liu v. S.E.C.*, the Supreme Court agreed to hear an appeal challenging whether the Commission has statutory authority to seek disgorgement.⁹ In *Kokesh*, the Court in a footnote expressly declined to reach that issue. Separately, the U.S. House of Representatives Financial Services Committee recently passed, with overwhelming bipartisan support, a bill that would reverse *Kokesh* and grant the Commission statutory authority under the Securities Exchange Act of 1934 to seek disgorgement for up to 14 years in civil enforcement actions.¹⁰

* * *

Please do not hesitate to contact us with any questions.

⁹ *S.E.C. v. Liu*, 754 F. App’x 505 (9th Cir. 2018), *cert granted sub nom. Liu v. SEC*, 2019 WL 5659111 (U.S. Nov. 1, 2019) (No. 18-1501).

¹⁰ See H.R. 4344, 116th Cong. (2019), <https://www.congress.gov/bill/116th-congress/house-bill/4344/>

WASHINGTON, D.C.



Kara Brockmeyer
kbrockmeyer@debevoise.com



Robert B. Kaplan
rbkaplan@debevoise.com



Arian M. June
ajune@debevoise.com



Julie M. Riewe
jriewe@debevoise.com



Jonathan R. Tuttle
jrtuttle@debevoise.com



Ada Fernandez Johnson
afjohnson@debevoise.com



Ryan M. Kusmin
rmkusmin@debevoise.com

NEW YORK



Andrew J. Ceresney
aceresney@debevoise.com



Mary Jo White
mjwhite@debevoise.com



James B. Amler
jbamler@debevoise.com