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SEC Enforcement – Deterrence, Prevention or Both?

The Commission's current enforcement approach was detailed by Chair Mary Jo White in a speech delivered to the Australian Securities Investment Commission. In remarks titled "Perspectives on Strengthening Enforcement," delivered on March 24, 2014 (here), Ms. White discussed first the necessity for international cooperation in enforcement and then the Commission's current approach to enforcement.

The critical points regarding the SEC's new "get tough" enforcement approach articulated by Ms. White to the ASIC are, by now, familiar themes to those who follow the agency. The central focus is deterrence, utilizing the tools available to the Commission, a theme drawn from Ms. White's time as the U.S. Attorney in Manhattan. Establishing what she calls an "undeniable message of deterrence" is the reason the SEC Chair supports statutory changes to increase the maximum penalties the agency can impose. While the penalties which can be imposed at present "can be quite high, it still frequently falls far short of the amount of investor losses." Presumably, larger dollar figures which match those of the losses would have more deterrent effect in the market place – at least that seems to be the theory.

A critical component of the deterrence message comes from working in parallel with criminal authorities who can "jail wrongdoers and obtain higher monetary penalties." While the SEC cannot jail violators it can use its "very powerful non-monetary sanctions" such as the authorities to bar wrongdoers from the securities business or from serving as an officer or director of a public company for a period of years. Bars can also be used to preclude a lawyer or accountant from practicing before the Commission, thus presumably achieving deterrence. Striking another criminal theme, Ms. White summed up the SEC's approach as imposing sanctions that "have teeth so that the punishment comes as close as our authority allows to fit the crime."

A key feature of the new enforcement policy, the Australian regulators were told, is the admission's policy. This is another way in which the SEC is holding firms accountable while "boosting investors' confidence" the SEC Chair noted. Thus where there is "egregious" conduct admissions will be required. Ms. White cited the actions against hedge fund mogul Philip Falcone and the settlement involving JPMorgan as examples of the kind of conduct where this policy applies. She did not mention the action against Scottrade where admissions were required to settle a case in which the firm had a computer coding error that resulted in the incomplete productions of blue sheets – documents containing trading data – to the staff. *In the Matter of Scottrade, Inc.,* Adm. Proc. File No. 3-15702 (Jan. 29, 2014).

Prosecuting gatekeepers and small violations – two more familiar themes – are also key facets of the current enforcement policy. Citing a settled action against a group of mutual fund directors in which part of the charges were dropped in settlement, "Operation Broken Gate" and a release where three auditors from small firms were charged, Ms. White insisted that the SEC will ensure that "gatekeepers understand their special duties and responsibilities, and that they will be held accountable . ." Indeed, by prosecuting small violations "[w]e are trying to prevent smaller securities violations from becoming more serious ones . . ." another lesson from her time at the U.S. Attorney's office.

Not mentioned in all the talk about deterrence was measures to protect investors and the markets from a reoccurrence of wrongful conduct in the future. The SEC Chair insisted that "our philosophy is to use all of the tools in our enforcement arsenal . . ." Yet nothing was said about ancillary relief, a topic little mentioned these days. Nothing was said about the traditional SEC approach of fashioning remedies tailored to the specific situation to ensure that the markets and public are protected from a replication of the wrongful conduct in the future. Traditionally it has been the creative, and very effective use of such relief, that has made the SEC enforcement program very successful at protecting investors and the markets.

Borrowing themes from criminal prosecutors, such as deterrence, may have a place in SEC enforcement. It is critical, however, that time tested remedies not be lost in the rush to be achieve some form of deterrence through punitive measures such as big fines, admissions and bars from the securities or other businesses. The SEC is a civil regulator, not a criminal prosecutor. It is a protector of investors and the markets, not a jailor. It is critical that the agency recall this if it is going to fully implement its statutory mandate to protect the investing public and the markets.

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