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The Wells Process at the Conclusion of an SEC Investigation

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When the Staff has completed its investigative work and is preparing to submit its recommendations for enforcement action to the Commission, if the Staff believes it is appropriate to bring charges, the "Wells process" will begin. At this stage, the Staff informs prospective defendants or respondents of the charges under consideration, and invites them to present their defenses. The Wells process thus gives counsel an opportunity to impact the Staff's view of the case, the Staff's ultimate presentation of a recommendation to the Commission and the Commission's view of the matter.

The commitment of the Staff and the Commission to a meaningful Wells process has been a significant part of the foundation underlying the Commission's historical reputation as a "tough but fair" regulator. This process—which has become integral to the defense of enforcement matters—originated in decades-old informal practices.

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History of the Wells Process

Q 6.1 Why is it called the "Wells" process?

Before 1972, subjects of an SEC investigation were not generally advised that they could present a written statement advocating the merits of their position to the SEC. When enforcement recommendations were made by the Staff, the Commission in most instances relied solely on the Staff's investigatory results, with no input from the potential defendant or respondent. If, however, experienced defense counsel requested the opportunity to submit a written statement, the Staff would advise them of the potential charges and permit a written submission to be made. As a result, veterans of the regulatory process often benefited from the opportunity to file written rebuttals to contemplated charges, while neophyte counsel never realized that it was possible to present their client's position to the Commission before charging decisions were made.[1]

On January 27, 1972, then-SEC Chairman William J. Casey appointed John Wells and two others to an Advisory Committee (called the "Wells Committee") to review the Commission's enforcement policies and practices. The Committee issued a report in June 1972.[2] Among other things, the report noted that, "[a]lthough the staff will in some cases advise an attorney of the opportunity to submit his client's contentions, these procedures are generally followed only if the attorney takes the initiative in requesting that his client's views be submitted

to the Commission. As a practical matter, only experienced practitioners who are aware of the opportunity to present their client's side of the case have made general use of these procedures."[3] Motivated at least in part by a desire to make the entire enforcement process fairer, the Committee's report recommended that the practice of advising prospective defendants of the opportunity to make a submission to the Staff should be broadly available and publicized in a rule or SEC release:

> [A] prospective defendant or respondent should be notified of the substance of the staff's charges and probable recommendations in advance of the submission of the staff memorandum to the Commission and be accorded an opportunity to submit a written statement to the staff which would be forwarded to the Commission together with the staff memorandum. Where such an opportunity has not been afforded, the staff memorandum should so indicate and the reasons therefor. We suggest, however, that the Commission impose appropriate limitations on the number of pages allowed in the adverse party's statement and on the time within which it could be submitted to the staff. In fairness to all persons who may become involved in Commission proceedings, however, we strongly recommend that the procedure adopted be reflected in a rule or published release.[4]

Q 6.2 What are the SEC's policies governing the Wells process?

Although the SEC declined to adopt a formal rule governing the giving of notice to a prospective respondent or defendant of the Staff's charges and the opportunity to make a submission in advance, in September 1972, the agency issued a Release notifying the public for the first time of the informal practice of receiving submissions. Over four decades later, the Staff still includes a copy of this Release with each Wells notice it sends out.[5]

SOME HISTORY: The 1972 Wells Release

"The Commission, however, wishes to give public notice of a practice, which it has heretofore followed on request, of permitting persons involved in an investigation to present a statement to it setting forth their interests and position. But the Commission cannot delay taking action which it believes is required pending the receipt of such a submission, and, accordingly, it will be necessary, if the material is to be considered, that it be timely submitted. In determining what course of action to pursue, interested persons may find it helpful to discuss the matter with the staff members conducting the investigation. The staff, in its discretion, may advise prospective defendants or respondents of the general nature of its investigation, including the indicated violations as they pertain to them, and the amount of time that may be available for preparing a submission. The staff must, however, have discretion in this regard in order to protect the public interest and to avoid not only delay, but possible untoward consequences which would obstruct or delay necessary enforcement action."

A briefer version of the Release was subsequently published in the Commission's informal rules:

> Persons who become involved in preliminary or formal investigations may, on their own initiative, submit a written statement to the Commission setting forth their interests and position in regard to the subject matter of the investigation. Upon request, the staff, in its discretion, may advise such persons of the general nature of the investigation, including the indicated violations as they pertain to them, and the amount of time that may be available for preparing and submitting a statement prior to the presentation of a staff recommendation to the Commission for the commencement of an administrative or injunction proceeding.
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> In the event a recommendation for the commencement of enforcement proceeding is presented by the staff, any submissions by interested persons will be forwarded to the Commission in conjunction with the staff memorandum.[6]

Q 6.3 Does the Enforcement Manual address the Wells process?

The SEC Enforcement Manual, made publicly available for the first time in October 2008, reaffirms the policy articulated in Release No. 5310 and notes that the Staff should refer back to the intent of the original "Wells Release" in making determinations regarding Wells notices.[7] The Manual contains a definition of a Wells notice:

> A Wells notice is a communication from the staff to a person involved in an investigation that: (1) informs the person the staff has made a preliminary determination to recommend that the Commission file an action or institute a proceeding against them; (2) identifies the securities law violations that the staff has preliminarily determined to include in the recommendation; and (3) provides notice that the person may make a submission to the Division and the Commission concerning the proposed recommendation.[8]

The Manual restates the objective of the Wells notice: "to not only be informed of the findings made by its staff but also, where practicable and appropriate, to have before it the position of persons under investigation at the time it is asked to consider enforcement action." The Manual further details exactly what the notice should contain. It specifies that the notice should inform a person involved in an investigation that:

> 1) The Division is considering recommending or intends to recommend that the Commission file an action or proceeding against them; 2) the potential violations at the heart of the recommendation; and 3) the person may submit arguments or evidence to the Division and the Commission regarding the recommendation and evidence.

The Staff is required to obtain the approval of an Associate Director or Regional Director before issuing a Wells notice or determining to recommend an enforcement action without issuing a Wells notice.[9]

The senior official's determination to authorize the Wells notice is based upon a briefing from the investigative team concerning the results of their investigation. While that briefing is frequently presented in writing, in some cases it may be presented orally. While there is no formal opportunity afforded to defense counsel to be heard on the question of whether a Wells notice will be issued, in some cases it may be advisable to reach out proactively to the Staff when an investigation appears to be concluding in order to present the defense's perspective on the case before the Wells decision is made.

Learning of a Wells Notice

Q 6.4 How does the Staff deliver a Wells notice?

The Enforcement Manual states that a Wells notice should be in writing when possible. The Manual also provides that if the Staff intends to provide a written Wells notice, "the staff may give advance notice of the intention to the recipient or his or her counsel by telephone." During this call, the Staff may "refer to specific evidence regarding the facts and circumstances which form the basis for the staff's recommendations."[10] Most commonly, the Staff places a "Wells call" to defense counsel, followed shortly thereafter by the written notice.

Generally, defense counsel should engage in a dialog with the Staff during the Wells call, beginning the process of seeking to learn as much as possible about the Staff's views, the specific charges under consideration and the evidence that the Staff believes would support an enforcement action. This discussion on the Wells call, however, should not be viewed as the only opportunity for such interchange with the Staff. The Staff is usually amenable to a later meeting or phone call in which defense counsel may pose additional questions after having more of an opportunity to think through the implications of the Wells notice.

Q 6.5 What information is contained in a written Wells notice?

The Manual specifies precisely what should be contained in the written Wells notice or confirmation of an oral Wells notice. The notice should:

- identify the specific charges the Staff is considering recommending to the Commission;
- accord the recipient of the Wells notice the opportunity to provide a voluntary statement, in writing or on videotape, setting forth the recipient's position with respect to the proposed recommendation, which in the recipient's discretion may include arguments why the Commission should not bring an action or why proposed charges or remedies should not be pursued, or bring any relevant facts to the Commission's attention in connection with its consideration of the matter;
- set reasonable limitations on the length of any submission made by the recipient (typically, written submissions should be limited to forty pages, not including exhibits, and video submissions should not exceed twelve minutes), as well as the time period allowed for the recipients to submit a voluntary statement in response to the Wells notice;
- advise the recipient that any submission should be addressed to the appropriate Assistant Director;
- inform the recipient that any Wells submission may be used by the Commission in any action or proceeding that it brings and may be discoverable by third parties in accordance with applicable law;
- attach a copy of the Wells Release, Securities Act Release No. 5310; and
- attach a copy of the SEC's Form 1662 ("Supplemental Information for Persons Requested to Supply Information Voluntarily or Directed to Supply Information Pursuant to a Commission Subpoena").[11]

Most of what appears in a written Wells notice is boilerplate. Typically, the written notice identifies the statutory and rule violations under consideration, but contains no reference to the facts of the specific case. Consequently, discussions with the Staff are essential to obtain a better understanding of the charges under consideration and the factual and legal basis for them. As noted above, the Enforcement Manual provides that the notice should specify that Enforcement is "considering recommending or intends to recommend" that the

Commission commence an action or proceeding. While the language on its face suggests there may be some substantive difference between these two formulations, experience and anecdotal evidence have not borne this out.[12]

The Wells Schedule and Procedure

Q 6.6 How does the Dodd-Frank deadline affect the Wells process?

Section 929U of the Dodd-Frank Act imposes certain time constraints on the SEC in connection with the Wells process. Section 929U provides that within 180 days of issuing a Wells notice, the Commission "shall either file an action against such person or provide notice to the Director of the Division of Enforcement of its intent not to file an action."[13] The section also allows for an extension for one or more additional successive 180-day periods if the Director of Enforcement determines that a particular investigation is "sufficiently complex."[14]

The expiration of this statutory deadline, however, will not necessarily bar the filing of an enforcement action. The United States Court of Appeals for the D.C. Circuit has ruled that these time limits create an internal timing directive rather than a jurisdictional bar to an action.[15] In *Montford*, the Petitioners challenged an order imposing sanctions for violations of the Investment Advisers Act, arguing, among other things, that the enforcement action was untimely under section 4E of the Exchange Act because the SEC waited 187 days after issuing a Wells notice before it instituted administrative proceedings. In reviewing the ALJ's decision, the Commission construed section 4E for the first time, holding that "dismissal of an action is not the appropriate remedy when the time periods set forth in Section 4E are exceeded." The Commission noted that the statute is silent on the consequences for noncompliance and that courts have historically been reluctant to read in a jurisdictional bar for failure to comply with an internal deadline for federal agency action. The D.C. Circuit upheld the Commission's construction as reasonable and entitled to deference, and thus did not even consider the SEC's alternative argument that it had properly extended the deadline.

Section 929U was enacted with the goal of providing closure to the Wells process within a fixed time frame. The provision allowing

for extensions of the 180-day time limit, however, is a critical feature. In many cases, it is in the interest of prospective defendants and of the Commission—indeed, in the public interest—for a Wells process to extend well beyond 180 days. If counsel raise valid defenses, the enforcement process benefits from the Staff having adequate time to consider those defenses. In some cases, defense arguments presented during the Wells process prompt the Staff to undertake further investigation. Additional written submissions and oral presentations by defense counsel may be appropriate following completion of the Staff's further investigation. All of these steps take time, and 180 days can pass very quickly.

Q 6.7 When does the Staff decline to give a Wells notice?

As the Commission's policy statements reflect, the decision to provide a Wells notice is within the Staff's discretion. In practice, the Staff determines to provide Wells notices in most cases. In general, the exceptions are cases in which there is a danger that providing the notice would be contrary to the public interest or interfere with the administration of justice. Thus, the Staff typically does not provide Wells notices in cases in which the Staff anticipates seeking emergency relief such as an asset freeze (for example, in a case involving an ongoing Ponzi scheme), or cases in which the Staff anticipates parallel criminal charges and a pre-arrest Wells notice would create a flight risk.

Obtaining Information After the Wells Notice

Q 6.8 How transparent is the Staff about evidence and theories?

Once a Wells notice has been received, counsel typically will want to reach out to the Staff informally. The Staff's willingness to discuss its views of the case and the evidence varies somewhat from office to office, and even among groups in the same office. It is critical to an effective Wells process to learn as much as possible about the Staff's understanding of the case. Counsel should focus especially on understanding the evidentiary basis that the Staff believes would support an enforcement recommendation. Counsel should also ask the Staff to articulate its legal theories. Obtaining this information puts counsel in

the best position to prepare a Wells submission that addresses the issues that are in fact important to the Staff's thinking. For this reason, it is generally advisable to be persistent in trying to have a dialog with the Staff about its views of the case, the evidence and the potential charges.

Reviewing evidence and testimony that the Staff has gathered from other parties can also be enormously useful. In appropriate cases, counsel should ask for access to these materials. In pressing this request, counsel will need to articulate convincing reasons why the enforcement process will be advanced if the Staff provides access. The Enforcement Manual clarifies that, on a case-by-case basis, it is within the Staff's discretion to allow the recipient of a Wells notice to review portions of the investigative file that are not privileged. In considering a request for access to portions of the Staff's investigative file, the Staff is instructed to keep in mind, among other things:

- whether access to portions of the file would be a productive way for both the staff and the recipient of the Wells notice to assess the strength of the evidence that forms the basis for the staff's proposed recommendations;
- whether the prospective defendant or respondent failed to cooperate, invoked his Fifth Amendment rights, or otherwise refused to provide information during the investigation; and
- the stage of the investigation with regard to other persons or witnesses, including whether certain witnesses have yet to provide testimony, and whether there is a parallel criminal or regulatory investigation or proceeding that may be adversely affected by granting access to the staff's file.[16]

Disclosure of a Wells Notice

Q 6.9 Is a public company required to disclose receipt of a Wells notice?

A Wells notice is a non-public communication to the recipient, and the notice will not be made public by the Commission. Historically, companies rarely made public disclosure of their receipt of a Wells notice. In recent years, however, increasing numbers of companies

have more frequently elected to disclose the receipt of a Wells notice. Generally, such disclosures are a discretionary choice, rather than a requirement. Indeed, a federal district court in the Southern District of New York held in June 2012 for the first time that there is no duty for companies to disclose publicly the receipt of a Wells notice.[17]

In *Richman v. Goldman Sachs*, private plaintiffs alleged that Goldman violated § 10(b) of the Exchange Act and Rule 10b-5 by failing to disclose its receipt of a Wells notice from the SEC. Plaintiffs claimed both that Goldman had an affirmative obligation to disclose receipt of the Wells notice, and that disclosure was required in order to prevent its prior disclosures about the government's investigation from being misleading. The court rejected these claims. With respect to the general duty to disclose, the court found that there was nothing in the SEC rules explicitly requiring disclosure of a Wells notice. "When the regulatory investigation matures to the point where litigation is apparent and substantially certain to occur, then 10(b) disclosure is mandated. . . . Until then, disclosure is not required."[18]

The court similarly rejected plaintiffs' claim that Goldman's prior disclosures that the government was investigating Goldman's synthetic CDO mandated disclosure of the Wells notice. Noting that the Wells notice indicated only that the investigations were ongoing, and that it reflects "not litigation but only the desire of the Enforcement staff to move forward," the court held that this "contingency" need not be disclosed.[19] The court's reasoning is consonant with the true nature of a Wells notice. A Wells notice is not commencement of a legal proceeding, it does not constitute the bringing of charges, and it does not represent a conclusion by the Commission or its Staff that charges would be appropriate. As noted above, a substantial number of Wells notices do not ever lead to commencement of an enforcement action against the recipient. In another very recent case raising the same issue, the Southern District of New York, citing *Richman*, reconfirmed that there is no duty to disclose the existence of an SEC investigation or the receipt of a Wells Notice because the securities laws do not impose an obligation to predict the outcome of investigations.[20] Chapter 9 of this book addresses disclosure issues in detail.

Q 6.10 Are registered persons in the securities industry required to disclose receipt of a Wells notice?

The receipt of a Wells notice must, however, be disclosed on a Form U-4. Thus, the same Wells notices that formed the basis for the *Richman* plaintiffs' claims ultimately led to FINRA sanctions against Goldman.[21] Goldman's violation was its failure to update the Uniform Application for Securities Industry Registration or Transfer (Form U-4) to reflect the receipt of a Wells notice by two of its employees. Question 14G on the Form U-4 specifically asks:

> "Have you been notified, in writing, that you are now the subject of any
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> * * *
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> *(2) investigation* that could result in a "yes" answer to any part of 14A, B, C, D or E? (regulatory action by various agencies).

"Investigation" is defined to include SEC investigations when a written Wells notice has been given.

Preparing the Wells Submission

Q 6.11 Can a Wells submission really impact a charging decision?

Reported statistics reflect that making a Wells submission may, in fact, have a significant influence on the SEC's decision whether to take enforcement action. In the two years ending September 2012, 797 Wells notices were issued to individuals.[22] Of those, 159 did not result in any enforcement action.[23] Former Chair Mary Schapiro stated that the numbers demonstrate that the system works: "It's exactly what the Wells notices are intended to do: to bring out someone's best defense before a decision is made on whether to charge them."[24]

These statistics are consistent with the experience of practitioners. The senior Staff take the Wells process seriously, and are open to considering well-grounded defense arguments. On the defense side, while most Wells notices ultimately do lead to some form of

enforcement action, there are many cases in which there is a genuine opportunity for effective advocacy to persuade the Staff to narrow a charge or even close an investigation.

Q 6.12 What is the best approach to writing a Wells submission?

An effective Wells submission can accomplish many different objectives. The submission will not necessarily resemble a typical adversarial brief in private litigation. The goal of the Wells submission is to tailor the arguments to appeal to the discretion of the Staff. The submission should be directed to address the Staff's theory of the case, and designed to highlight any weakness or point out any undesirable consequences of their position.

Although Securities Act Release No. 5310 stressed that the Wells submission normally would be most useful in connection with issues of policy or law rather than questions of fact,[25] as a practical matter, most practitioners do not abide by this guidance and it is generally not wise to limit submissions in this fashion. While policy and legal arguments should be made if they are helpful, the factual portion of the Wells submission is often the most important. If the Staff is relying on an understanding of the facts that is not supported by—or contrary to—the evidentiary record, it can be critically important to make that clear in the Wells submission. The Staff's investigations tend understandably to focus on inculpatory evidence. The Wells submission can be an important vehicle to call the Staff's attention to exculpatory evidence that the Staff overlooked or chose not to develop in the investigation. It is equally important that any factual statements made in the Wells submission be accurate and well-supported by evidence. A Wells submission must be credible in order to be effective.

The Wells submission should briefly state counsel's understanding of the charges under consideration, and the facts identified by the Staff as supporting the prospective charges. In the event that the Staff changes any aspect of its recommendation as a result of the Wells process, this summary will put the reader of the submission on notice that defense counsel has not had an opportunity to respond to the revised theory of the case.

In considering how to frame a Wells submission, it is frequently useful to focus on the legal elements that the Commission would be required to prove to establish the violations at issue. For example, the Staff may have strong evidence that a false statement was made, but may lack proof that it was made with the requisite level of intent, or that it was material. Focusing on the required elements is another way to identify potential gaps in the Staff's investigation.

Q 6.13 Should I consider making a video Wells submission?

As noted above, a written Wells notice informs the recipient of the option of making a video Wells submission, limited to twelve minutes. In most cases, any temptation to take up this invitation should be resisted. Video submissions are rare, and they are seldom, if ever, effective. An effective Wells submission will engage substantively and in detail with the evidence and issues in the case, an approach that is not well-suited to video, as opposed to a written submission that the Staff can focus on and consider carefully.

Q 6.14 Who will read the Wells submission?

When drafting the submission, it is important to focus on who the audience will be. A number of different personnel at the Commission will likely have an opportunity to review the submission. Generally, it is most difficult to change the views of the Staff directly handling the investigation, who have developed their own theories of the case and who have typically devoted extensive time and energy to supporting those theories. But the submission will also be reviewed by more senior Staff who supervise the line attorneys and have less personal familiarity with the evidentiary record. More senior Staff may come to the case with more critical distance and objectivity than the Staff who have spent months or years pursuing the investigation. This again underlines the importance of preparing a credible submission that squarely addresses the most challenging issues in the case.

Enforcement recommendations are also reviewed by other interested divisions and offices (for example, Corporation Finance and the Office of Chief Accountant review all accounting and financial reporting cases; Trading and Markets reviews all broker-dealer cases; Investment

Management reviews all Advisers Act cases, etc.). The Commission's Office of General Counsel (OGC) reviews all enforcement recommendations. In a given case, the policy concerns or programmatic interests of an interested division or office may be appropriate to address in the Wells submission. In addition, the specialized divisions or offices may bring greater expertise to the issues arising in their program areas.

If the Staff determines to proceed with an enforcement recommendation and there is no settlement, the Wells submission will also be provided to each of the Commissioners and their personal staff and legal advisors. At the same time, the Commissioners will receive a non-public "action memo" from the Staff detailing the factual and legal basis for the recommendation. The action memo is written by the Staff and reviewed by the other interested divisions and offices before going to the Commissioners. The action memo will include the Staff's response to the Wells submission, which defense counsel do not have an opportunity to see or reply to.

Q 6.15 What makes a Wells submission effective?

Each case is unique, and the most effective approach will turn on the strengths and weaknesses of the case. No submission will be effective, however, if it fails to come to grips with the merits of the enforcement recommendation that the Staff is considering. Typically, submission of supporting documents and citation to testimony add to the force and persuasiveness of the written submission. While the submission should set forth the defense's most powerful arguments, it should also confront and address any issues that are problematic from the defense perspective.

In order to have its desired impact, a Wells submission must be credible. Facts should not be overstated, controversial factual arguments should be well-supported and legal arguments should be well-grounded. Any misstatement will be noted by the Staff and will detract from the credibility of the submission—and will be highlighted by the Staff in its action memo to the Commission.

A Wells submission need not cover the waterfront in order to be effective. It is not necessary to attempt to refute every one of the Staff's factual contentions. In many cases, a targeted submission can be more effective. For example, in a disclosure case, it may be sufficient to make

a persuasive demonstration that the maker of the statements acted in good faith (without fraudulent intent). In an insider trading case, showing that there was no breach of duty involved in the communication of non-public information may be sufficient. In short, if there is a fatal flaw in the Staff's case—such as an inability to prove a required element—a submission that is highly persuasive on that point may be the most effective.

An expert report may add to the effectiveness of a Wells submission. This is another case-by-case question. Defense counsel should consider what aspect of the investigation might be addressed by an expert. An expert opinion can be very helpful, for instance, if it directly addresses the Staff's inability to prove a required element of the violation. In an accounting case, assistance from a forensic accountant may be indispensable. By contrast, an expert report will not be helpful if it addresses a matter that the Staff views as collateral to the case, or if it is not credible because it relies on questionable factual assumptions.

Q 6.16 Should counsel ever decline to make a Wells submission?

There are instances when it may not be in the client's best interest to make a Wells submission. For example, if it appears likely that an acceptable settlement can be negotiated, it may not be worth incurring the effort and expense involved in preparing an effective Wells submission.[26]

Likewise, if there is a significant likelihood of litigation (including trial of a parallel criminal prosecution), it may not be in the defendant's best interest to make a submission. The Wells submission may be admissible and may reveal more about the defense's arguments and strategies than is desirable from a strategic perspective.

Q 6.17 Are Wells submissions admissible evidence in SEC and other proceedings?

In *In re Initial Public Offering Securities Litig.*,[27] Judge Scheindlin held that Wells submissions are not protected from discovery by third parties in subsequent civil litigation. The court characterized the matter as one of first impression although noting that, in *In re Steinhardt Partners, L.P.*,[28] defendant's voluntary Wells submission was held to

have waived work product protection as to subsequent civil litigants. The plaintiffs in the IPO litigation alleged that the defendants, several investment banks, required their customers to buy shares of stock in the aftermarket as a condition of receiving initial public offering stock allocations.[29] Prior to the commencement of litigation, both the SEC and the U.S. Attorney's Office for the Southern District of New York had begun investigations into the IPO allocation and commission process. Eventually, after serving subpoenas on the banks and receiving information on the banks' underwriting practices, the SEC sent Wells notices to certain of the investment banks, notifying them that it was considering charging them with violations of the Securities Act.[30] The civil plaintiffs sought discovery of the banks' Wells submissions. The defendants objected to the production of the Wells submissions, arguing that they constituted settlement materials, discovery of which would require a "particularized showing of relevance."[31] Judge Scheindlin rejected that argument and concluded that Wells submissions are not settlement materials. She noted that "offers of settlement . . . are not intrinsically part of Wells submissions, which were intended to be 'memoranda to the SEC presenting arguments why an enforcement proceeding should not be brought.'"[32] Judge Scheindlin also stressed that to the extent a settlement offer is actually contained in a Wells submission, the offer is usually clearly identifiable and can be redacted from the submission.[33] Finally, the Judge concluded that the scope of permissible discovery is not limited by Federal Rule of Evidence 408 restricting the admissibility of settlement materials, and that the submissions were clearly relevant to the litigation, having been "drafted precisely to address, and rebut, the same charges that plaintiffs raise here."[34]

The Commission takes the position that statements in a Wells submission can be used against the defendant in subsequent proceedings under Federal Rule of Evidence 801(d)(2), either as a statement against interest or for purposes of impeachment.

Q 6.18 Can the Staff reject a Wells submission?

In an October 2016 amendment to section 2.4 of the Enforcement Manual, the Commission specified four specific instances in which the Staff may reject a Wells submission. A submission may be rejected if: (1) it exceeds the length specified in the Wells notice; (2) it is submitted

after the deadline imposed by the Staff, including any extensions; (3) the person making the submission seeks to limit its admissibility under FRE 408 or the Commission's ability to use it for purposes described in Form 1662; and (4) the submission contains or discusses a settlement offer. The Manual states that Wells submissions that are rejected on any of these grounds generally will not be provided to the Commission.[35]

Process Following a Wells Submission

Q 6.19 What is a Wells meeting?

Interaction with the Staff continues after the Wells submission is filed. It is typically in the defendant's interest to contact the Staff and request a meeting. Typically, counsel will make an oral presentation, and the Staff will interject questions or comments. A Wells meeting can be helpful in a number of respects. It can give defense counsel another opportunity to ensure that the Staff fully understands the facts and the defendant's view of the case. Counsel may glean new insights into the Staff's approach to defense arguments and/or learn that the Staff may have altered its approach in response to the arguments presented in the Wells submission. Depending on the issues, counsel may want to request that representatives of other interested divisions or offices attend.

Counsel should view the meeting as a critical opportunity to try to assess and further impact the Staff's view of the case. Counsel should welcome questions and dialog with the Staff during the meeting, as these interchanges present further opportunities to understand the Staff's view of the case. Multiple Wells meetings are sometimes available, although the Dodd-Frank time limits sometimes place some pressure on this stage of the process.[36]

It is sometimes advantageous to prepare a supplemental written submission subsequent to meeting with the Staff. This writing might address a perceived change in the Staff's position or simply address particular areas of concern arising at the meeting.

Q 6.20 Does issuance of a Wells notice prevent the Staff from conducting further investigation?

Issuance of a Wells notice does not impose any limit on the Staff's ability to conduct further investigation. A Wells submission may show the Staff that their evidence is not as strong as they believed, or that there are relevant facts that the investigation failed to develop. This may prompt the Staff to investigate further to fill these gaps. The Staff may also conduct further investigation to test new factual assertions contained in the Wells submission.

Q 6.21 Can the Wells process lead to settlement negotiations?

The Wells process can, at any stage, transition to a settlement negotiation. Often, receipt of a Wells notice will prompt the prospective defendant to consider whether to pursue a settlement. In a case in which there is a substantial risk of liability, there may be an early decision to open settlement negotiations rather than proceed with a Wells process.

In other cases, proceeding with a Wells process may be part of a strategy that contemplates at some point moving into a settlement negotiation. Even if an eventual settlement is a distinct possibility, it may well be in the client's interest first to pursue the Wells process. Even if the Staff cannot be persuaded to close the investigation, the Wells process may favorably impact the Staff's view of the evidence, and may persuade the Staff to narrow the case, either by dropping some of the contemplated charges, or by revisiting the factual basis for the charges. In short, the dialog, written submissions and oral presentations in the Wells process may help position the case for settlement on terms that are more palatable—and more fair and appropriate—than the terms initially envisioned by the Staff.

Counsel has the ability to initiate settlement discussions at any point before the Staff's enforcement recommendation is presented to the Commission. Settlement discussions can also occur after the Commission has acted on an enforcement recommendation, but the opportunity for any amelioration of the charges is vastly reduced once the Commission has considered and authorized the case.

The "Pre-Wells" Process

Q 6.22 What is a "pre-Wells" process?

In some cases, the Staff is willing to engage in dialog with defense counsel, at the conclusion of an investigation, but before issuing a Wells notice. When this occurs, it is often referred to as a "pre-Wells" process. It may include written submissions (or "white papers") and oral presentations by defense counsel.

The Staff may be willing to engage in a pre-Wells process if a case involves novel or highly technical issues, or significant policy questions. In some cases, the Staff is willing to allow a pre-Wells process because they believe it will facilitate reaching a settlement. Finally, there may be extenuating circumstances in a particular case that cause the Staff to be willing to proceed on a pre-Wells basis.

The practice of engaging in a pre-Wells process has been in existence for many years, and predated the enactment of section 929U of Dodd-Frank, with its 180-day time limit. Since the enactment of section 929U, there has been some increase in the availability of a pre-Wells process, particularly in cases in which the Staff recognizes the advantage of an opportunity to explore the issues in a particular investigation with thoroughness and care, and without artificial time pressure.

The Enforcement Manual now clarifies, in a new section 3.2.3.2 added in October 2016, that during an investigation, a person may voluntarily produce to the Staff materials other than in response to a Wells notice, including white papers, PowerPoint decks, legal memos or letter briefs (collectively referred to as "White Papers"). As with the recently added provision regarding the Staff's ability to reject a Wells submission, the Staff may reject a White Paper if: (1) the person making the submission seeks to limit its admissibility under FRE 408 or the Commission's ability to use it for any purpose described in Form 1662; or (2) the White Paper contains or discusses a settlement offer.[37]

Notes to Chapter 6

1. *In re* Initial Pub. Offering Sec. Litig., 2003 U.S. Dist. LEXIS 23102 (S.D.N.Y. Dec. 24, 2003).
2. SEC, Report of the Advisory Committee on Enforcement Policies and Practices (June 1, 1972).
3. *Id.* at 31.
4. *Id.* at 32.
5. Procedures Relating to the Commencement of Enforcement Proceedings and Termination of Staff Investigations, Securities Act Release No. 5310, 1972 SEC LEXIS 238, at *3–4 (Sept. 27, 1972).
6. SEC Enforcement Activities, 17 C.F.R. § 202.5(c) (2004).
7. ENFORCEMENT DIV., SEC, SEC ENFORCEMENT MANUAL § 2.4 (2016), www.sec.gov/divisions/enforce/enforcementmanual.pdf.
8. *Id.*
9. *Id.*
10. *Id.*
11. *Id.*
12. The definition of a Wells notice in the Enforcement Manual contains a slightly different formulation—the Staff has made a preliminary determination to recommend that the Commission file an action. *See supra* Q 6.2.
13. Dodd-Frank Act § 929U, "Deadline for Completing Examinations, Inspections and Enforcement Actions."
14. *Id.*
15. Montford and Co. Inc. v. S.E.C., 793 F.3d 76 (D.C. Cir. 2015); *see also* SEC v. Nir Grp., LLC et al., No. 11-CV4723, 2013 WL 5288962 (E.D.N.Y. Mar. 24, 2013) (similarly finding that the time limits do not create a jurisdictional bar).
16. SEC ENFORCEMENT MANUAL, *supra* note 7, § 2.4.
17. Richman v. Goldman Sachs Grp. Inc. et al., 2012 WL 2362539 (S.D.N.Y. June 21, 2012).
18. *Id.*
19. *Id.* If a Wells notice renders earlier disclosures materially misleading or false, that might trigger a duty to make disclosure.
20. *See In re* Lions Gate Entertainment Corp. Sec. Litig., 14-CV-5197 (JGK), 2016 WL 29722 (S.D.N.Y. Jan. 22, 2016) ("A government investigation, without more, does not trigger a generalized duty to disclose.").
21. *See* FINRA, Letter of Acceptance, Waiver and Consent No. 2010 022 4738-01 (Oct. 18, 2010).
22. Jean Eaglesham, *SEC Drops 20% of Probes After Wells Notice,* WALL ST. J. (Oct. 9, 2013), www.wsj.com/articles/SB10001424052702304500404579125633137423664.

23. *Id.* The SEC does not appear to have compiled similar statistics with respect to corporations.
24. *Id.*
25. *See supra* note 5.
26. *See* Evan Stewart, *SEC 'Wells' Process Is a Bad Bet*, N.Y. SUN (June 2, 2008), www.nysun.com/opinion/secs-wells-process-is-a-bad-bet/79057/.
27. *In re* Initial Pub. Offering Sec. Litig., 2003 U.S. Dist. LEXIS 23102 (S.D.N.Y. Dec. 27, 2003).
28. *In re* Steinhardt Partners, L.P., 9 F.3d 230, 236 (2d Cir. 1993).
29. *In re* Initial Pub. Offering Sec. Litig., 2003 U.S. Dist. LEXIS 23102, at *7.
30. *Id.* at *7–8.
31. *Id.* at *10.
32. *Id.* at *13–14 (citing *In re* Towers Fin. Corp. Noteholders Litig., 1995 U.S. Dist. LEXIS 21147 (S.D.N.Y. Sept. 20, 1995)).
33. *Id.* at *15.
34. *Id.* at *27.
35. SEC ENFORCEMENT MANUAL, *supra* note 7, § 2.4.
36. *See* Sec. Litig. Grp., *SEC Speaks 2012*, NAT'L L. REV. (May 22, 2012), www.natlreview.com/article/sec-speaks-2012.
37. SEC ENFORCEMENT MANUAL, *supra* note 7, § 3.2.3.2.