Securities Litigation REPORT

September 2010 ■ Volume 7 ■ Issue 8

Revisiting the SEC Corporate Penalty Policy

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The Securities and Exchange Commission's power to secure civil money penalties against a public corporation implicates, in the Commission's own words, "significant questions for our mission of investor protection,"[1] as these money penalties ultimately are borne by the corporation's current shareholders.[2] One decade ago, few could have imagined the size and frequency of the civil money penalties recently levied on public companies. Reports have been circulating that the SEC will consider revisiting its corporate penalty policy.[3] It is particularly important for the Commission to do so in light of the recently enacted Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"), which, among other things, touched on the penalty power and related issues without changing the substantive standards for when and at what level penalties should be imposed.[4] As the SEC reviews its corporate penalty policy, we strongly urge the Commission to consider several important changes to enhance the efficiency and effectiveness of corporate penalties in tune with the agency's mission to protect investors and the public interest.

For most of its history, the Commission had no authority to seek civil monetary penalties against individuals or corporations.[5] In 1990, the Securities Enforcement Remedies and Penny Stock Reform Act (the "Remedies Act")[6] authorized the SEC to seek in civil injunctive actions[7] and to impose in administrative proceedings (against regulated individuals or entities)[8] money penalties for violations of the major federal securities laws. In the ensuing decade, the Commission sparingly—only twice—obtained civil penalties in substantial amounts ($1 million and $3.5 million) against public companies.[9] As late as 2002, the "largest fine ever obtained by the SEC against a public company in a financial fraud case" was a $10-million civil penalty paid in a settlement by Xerox Corp.[10] The landscape of SEC penalties looks radically different today. As a former SEC commis-

CONTINUED ON PAGE 4

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sioner observed in 2006, "Today, a $10 million SEC penalty would probably be considered a 'victory' for most entities settling SEC fraud charges—multi-million dollar SEC settlements have become almost commonplace over the last few years."[11] In 2003, the SEC obtained a $750-million penalty against Worldcom.[12] Between 2002 and 2008, it secured penalties of $10 million or more against 115 parties, including 14 penalties exceeding $100 million.[13] In that same period, the SEC sought or imposed against individuals and corporations penalties of approximately $1.1 billion per year.[14]

In 2006, after admittedly exercising the penalty power for years with persistent internal disagreements and no "clear public view" about when or how such penalties would be assessed, the SEC promulgated a nine-factor framework (the "2006 framework") to guide its decision whether to seek penalties against *corporations*.[15] The Commission touted this corporate penalty framework—developed from its careful consideration of the Remedies Act "and the legislative history surrounding that statutory authority"—as a source of "clarity, consistency, and predictability."[16] In practice, however, the nine, broad-textured factors have left the SEC with unbridled discretion, while affording no transparency, little predictability and debatable consistency.

The SEC Enforcement Staff plays a pivotal role in the determination of penalties in settled cases. By contrast with litigated cases, in which the size of the penalty is determined by the court, in settled cases the Staff negotiates a proposed penalty (along with the other settlement terms) with defense counsel on the basis of what the Staff is willing to recommend to the Commission. The Commission exercises ultimate authority, and must approve the terms of each settlement. But a settlement offer has little chance of approval if it is not recommended by the Staff, and it is unusual for the Commission to reject a Staff recommendation. The Staff thus has broad scope to exercise its discretion in negotiating proposed penalties. This allocation of functions between the Commission and its Staff has generally worked well over time, as the Staff has a detailed knowledge of the facts of the case, and defense counsel are able to engage in advocacy and negotiate directly with the Staff, which there is no opportunity to do with the Commission.[17] For the Commission, Staff, and defense counsel, however, the effectiveness of the enforcement program would be significantly aided by additional penalty guidance that is more transparent, consistent and predictable than that applied in the 2006 framework.

The Dodd-Frank Act, signed into law by President Obama on July 21, underscores the importance of the Commission revisiting its corporate penalty policy. The 1990 Remedies Act empowered only the courts to impose monetary penalties against any individual or entity; the Commission, instead, was authorized to impose money penalties in its administrative proceedings only against *regulated* individuals and entities. Eliminating this constraint on the SEC's administrative reach, the Dodd-Frank Act authorizes the Commission in cease-and-desist proceedings to impose money penalties against *any* person, including any public company.[18]

Yet nothing in the Dodd-Frank Act alters the substantive elements established by the Remedies Act for the SEC's penalty authority. The legislative history of the Dodd-Frank Act is bereft of new commentary concerning the criteria for when penalties should be imposed, and the statute itself does not change the size of the penalty for each violation or the "tier" definitions already prescribed by the Remedies Act and accompanying regulations. As a result, the Commission is in a position to step forward to thoughtfully revisit its penalty framework in light of the sensible guideposts endorsed by Congress in the Remedies Act and most recently reaffirmed in principle by the SEC in its issuance of the 2006 framework.

It is vital that the SEC promulgate meaningful, transparent guidance concerning its decisions whether to seek penalties against corporations, and if so, in what amounts. The Commission, the Staff, and defense counsel all would benefit from such guidance. In our view, the SEC's demand for extremely large penalty amounts against public companies is ill-advised and reflects insufficient consideration of the objectives and limitations that shaped Congress's expansion of the SEC enforcement authority. Though the size of penalties has waxed and waned with the Commission's changing composition, such inconsistencies reveal the existing penalty policy's vulnerability to the perception that it is subject to political, media and public pressures.

In reviewing its penalty policy, the Commission should return to the four key principles, endorsed by the SEC and Congress, that fueled the passage of the Remedies Act:

1. A civil money penalty against a corporation is not necessary in every case, particularly where violations occurred despite the company's reasonable compliance measures intended to prevent such violations.

2. A penalty should not be imposed on a corporation if it will be borne by injured shareholders or, due to turnover, innocent shareholders.

3. In exercising the penalty power, the SEC should maintain its remedial focus. While Congress has authorized the SEC to distribute to victims of securities law violations any disgorgement and penalty funds collected from companies, the opportunity to compensate investor losses was never intended to be a primary basis for the SEC to seek a corporate penalty. Injured investors are armed with private rights of action to recover losses; the SEC's principal enforcement missions have been, and remain, to prevent and deter violations, and to deprive the violator of ill-gotten gains.

4. The civil money penalty is but one tool in the SEC's enforcement arsenal that should be selectively deployed. In many circumstances, the Commission's nonpunitive remedial measures against corporations may be better suited to fulfill its enforcement mission.

Part I of this Article explores Congress's intent in granting the SEC the money penalty power, as well as the limitations promised by the SEC in requesting this authority. Part II examines the SEC's 2006 corporate penalty framework, and based on the Commission's and Congress's identical concerns in expanding the SEC's remedial arsenal, offers suggestions for the proper exercise of penalty authority. Finally, Part III discusses how deployment of the monetary penalty power against corporations should be harmonized with the SEC's other remedial tools.

Part I: The Roots and Limits of the SEC Corporate Penalty Power

In contemplating a penalty power for the SEC, a principal concern of Congress and expert witnesses alike was the assurance of meaningful limitations to this authority. In his subcommittee's first hearing on the proposed Remedies Act in 1990, Senator Christopher Dodd (D-Conn.) warned against his proposal's "unintended reach," emphasizing that the "SEC already has a tremendous arsenal of enforcement powers, ranging from administrative sanctions to the ability to refer matters for criminal prosecution."[19]

In fact, the Commission previously had rejected any need to supplement its existing remedies with monetary penalties beyond the context of insider trading.[20] Despite the "surface appeal" of such authority, the Commission worried that its marginal benefits would be outweighed by "a number of potentially serious disadvantages."[21] Civil monetary penalties, the Commission concluded, "might change the character" of its remedial enforcement program to a perceived punitive focus and "could also make it more likely that defendants… would litigate enforcement actions," thus hindering the SEC's "ability to settle enforcement actions" through "remedial relief to protect the investing public without" resort to full-blown litigation.[22] A remedial focus has historically been at the heart of the SEC enforcement program, as reflected in the regulatory functions it has performed:

- detecting wrongdoing;
- halting ongoing fraud;
- deterring future violations;
- recovering ill-gotten gains;
- removing unfit persons from the securities business, barring accountants and lawyers

who engage in improper professional conduct from appearing before the Commission, and barring unfit persons from serving as officers and directors of public companies; and

- encouraging corporate remediation.

These remedial functions all reflect the SEC's *regulatory* role of protecting investors and the public interest. Never did the SEC deem it a part of its mandate to "take sides" by pursuing compensation for investor losses, beyond what flowed from recovery of ill-gotten gains.[23]

Even once the SEC eventually sought the monetary penalty power,[24] worries persisted about its impact on the character and efficacy of the enforcement program. The SEC first sought penalty authority against individuals, but in its 1988 congressional testimony the Commission still requested more time to study "whether [civil] penalties should be imposed against corporate issuers under circumstances where shareholders will bear the costs of the penalty, and the procedures by which standards governing the size of civil monetary penalties should be established."[25] In ultimately seeking such authority against corporations, the Commission issued a SEC Memorandum that stressed to Congress several assurances:

- "First, the statute would not dictate that the Commission… seek… a penalty in any particular case. As a matter of enforcement policy, the Commission may proceed against the appropriate individual offenders acting for a corporate issuer, and would have the discretion not to seek penalties from an issuer."[26]

- "Second,… the Commission may properly take into account its concern that civil penalties assessed against corporate issuers will ultimately be paid by shareholders who were themselves victimized by the violations."[27]

Civil money penalties would be sought against corporations, the SEC underscored, "*only where the violation resulted in an improper benefit to shareholders*"[28]:

> **In a typical case of financial fraud in which a[n] issuer overstates it[s] earnings and revenues, for example, the only shareholders who reap a direct economic benefit are those who sell their shares at an inflated price before the fraud is exposed. By the time that an enforcement action is brought, a large percentage of the shareholders may consist of persons who purchased shares at a price that was artificially inflated as a result of the fraud. To assess a civil penalty in such a case against the issuer, as opposed to the individual officers who were responsible for the fraud, would appear to be inequitable.[29]**

In other cases, the SEC contended, "an issuer's violation does produce an economic benefit to shareholders" that justifies a corporate penalty: "The most common examples may be broker-dealer cases involving the failure to supervise sales practice activities, mark-up cases, and cases involving violations of the customer reserve provisions of the securities laws."[30] When the Remedies Act was under consideration, it bears noting, these examples largely did not involve public companies—they involved regulated entities that profited from violations, thus implicating the SEC's core function of regulating the securities industry and protecting customers of a broker-dealer. Today, by contrast, nearly all large broker-dealers either are public companies or are owned by public companies. Thus, even the limited "benefit to shareholders" examples cited by the SEC to justify a money penalty for the most part no longer exist.

The testimony of an array of active or former SEC officials echoed the SEC Memorandum's promised limitations on exercise of the penalty power. As Chairman of the Commission during the Remedies Act's consideration in Congress, Richard Breeden testified that the Commission "would not, of course, seek or impose a civil money penalty in every case":

> **Where a failure to comply with Commission requirements involves isolated or unintentional conduct, the implementation of new procedures or a similar remedial measure will often be the most appropriate resolution of the case. At the other end of the spectrum, where the defendant in**

a Commission action is also the subject of a criminal prosecution, the imposition of a civil money penalty in the Commission's action may not be needed to achieve deterrence.[31]

Similarly, the testimony of former SEC Enforcement Director Gary Lynch (a private practitioner at the time of his testimony) is illustrative of the cautions expressed to Congress:

- "[A] civil penalty authority should generally be exercised in those cases involving deliberate fraud and manipulation.... I think it is important for the Commission to maintain its historical focus on achieving remedial relief, rather than taking punitive action in every case, and that the Commission should still continue to judge the effectiveness of the Commission's enforcement program based on what it actually accomplishes, as opposed to what the dollar amount is that is ordered in a particular case."[32]
- "A civil money penalty should not become the *sine qua non* of all Commission enforcement actions. To put it another way, the Commission's historical focus on achieving remedial relief rather than taking punitive action should continue to provide the standard for evaluating the outcome of an enforcement action in most cases."[33]
- "The Commission should carefully examine whether those who ultimately have to pay the fine actually deserve to suffer a penalty.... [I]t would be 'inequitable' to assess a penalty against a corporate issuer in cases where the shareholders themselves have been victimized by the securities violations, given that such penalties are ultimately paid by the shareholders themselves."[34]
- "[A]s the Commission utilizes its penalty authority, more defendants and respondents will determine to litigate with the Commission rather than settle the case, if a settlement entails the payment of a large penalty. If the number of cases in litigation materially increases, there will be fewer staff members available to conduct investigations and thus the Commission's investigative 'coverage' of the securities markets will decrease unless Congress provides sufficient funds to hire additional lawyers, accountants, and analysts to make up for those diverted to a larger litigation workload."[35]

Finally, the House and Senate Committees—in nearly identical terms—relied upon the SEC assurances, as the following excerpts from the Committees' Reports demonstrate beyond cavil:

- "The Committee believes that the civil money penalty provisions should be applicable to corporate issuers.... However, *because the costs of such penalties may be passed on to shareholders, the Committee intends that the penalty be sought when the violation results in an improper benefit to shareholders*. In cases in which shareholders are the principal victims of the violations, the Committee expects that the SEC, when appropriate, will seek penalties from the individual offenders acting for a corporate issuer. Moreover, in deciding whether and to what extent to assess a penalty against the issuer, the court may properly take into account whether civil penalties assessed against corporate issue[r]s will ultimately be paid by shareholders who were themselves victimized by the violations. The court also may consider the extent to which the passage of time has resulted in shareholder turnover."[36]
- "The Committee contemplates that the SEC would not seek or impose a civil money penalty in every case. When a failure to comply with Commission requirements involves isolated or unintentional conduct, the implementation of new procedures or a similar remedial measure may be the most appropriate resolution of the case.... However, a person's disregard of the customer protection rules, the broker-dealer net capital rules, or repeated violations of recordkeeping requirements may warrant a money penalty."[37]

Thus, out of the legislative history to the Remedies Act emerge several unequivocal limitations on the Commission's proper exercise of the penalty power against corporations. SEC officials and legislators alike underscored that a penalty should not be borne by victimized shareholders or, due to turnover, innocent shareholders. The penalty was not to be used in every case, particularly where a reasonable compliance system failed. These limitations were deemed essential to the SEC's enforcement program, as overuse of the penalty power might hinder settlements and drain resources through increased litigation. The SEC should exercise its penalty power according to these carefully considered legislative objectives and limitations—fundamental guideposts that should not oscillate according to public sentiment or other outside pressures.

Part II: Clarifying Corporate Penalties

Greater focus must be given to when and how the corporate penalty power is exercised to be consistent with Congress's purposes in the Remedies Act. In its 2006 framework, the SEC specified two principal considerations for its determination whether a monetary penalty is appropriate against a corporation: (1) "The presence or absence of a direct benefit to the corporation as a result of the violation"; and (2) the degree to which the penalty "will recompense or further harm the injured shareholders." Additionally, the SEC noted seven further considerations: (1) The need to deter the particular type of offense charged; (2) the extent of the injury to innocent parties; (3) whether complicity in the violation is widespread throughout the corporation; (4) the level of the perpetrators' intent; (5) the degree of difficulty in detecting the particular type of offense; (6) the presence or absence of remedial steps taken by the corporation; and (7) the extent of the company's cooperation with the SEC and other law enforcement agencies.[38]

Clarifying "Principal Considerations"

The two principal considerations set forth in the 2006 framework for corporate penalties insufficiently reflect the authorizing statute's history and the agency's core remedial mission.

***Principal Consideration #1:* Direct Benefit to the Corporation**—The 2006 framework asks whether the "corporation itself" "benefited" from the violation. This focus on the benefit to the "corporation," however, strays from the SEC's and Congress's unambiguous focus on the *shareholders*—specifically, on whether shareholders were victims of the violation (or, through turnover, innocent of the violation) and therefore should not additionally bear the costs of penalties. The 2006 framework acknowledges that the "weakest case" for penalties is one in which shareholders are the principal victims of the violation. But the framework expressly endorses penalties based on corporate benefit through artificially "reduced expenses or increased revenues." That is directly contrary to the SEC's assurance to Congress that it would be "inequitable" to levy a penalty against a corporation based on such fraudulently reduced expenses or increased revenues alone.[39] The SEC and Congress recognized that the notion of a corporation's benefit through false financial reporting alone cannot provide the proper basis for a penalty that avoids harming shareholders who already are victims of the violation.

Even where false financial reporting makes possible a transaction from which the corporation benefits—for example, an acquisition[40]—it may not be true that "the shareholders" received an improper benefit. The only shareholders who directly benefited in such a case are those who sold their shares before the fraud was exposed, leaving among the current shareholders those who purchased shares at an artificially inflated price and those legacy shareholders who were injured as previous owners of the target company acquired through overvalued stock. As the SEC told Congress, to pursue a penalty that would be borne by those shareholders in such a case would be "inequitable."

Therefore, instead of emphasizing the question whether "the corporation" itself benefited from a violation, Congress directed the Commission to assess—among the host of other considerations described below—whether the shareholders themselves were victimized by the violation, given that penalties against the corporation are ultimately paid by the shareholders themselves.[41]

***Principal Consideration #2:* The Opportunity to Compensate Investor Losses**—The 2006 framework's attention to whether "the penalty will recompense" injured shareholders also misconstrues Congress's objective in the Remedies Act. Though this condition properly requires the SEC to consider whether a penalty will harm innocent, even injured shareholders, the 2006 framework goes further—it establishes that the "opportunity to use the penalty as a meaningful source of compensation to injured shareholders is a factor in support of its imposition." This reflects a potentially disturbing trend away from the SEC's historical *remedial* focus on investor protection, instead redirecting attention to compensation of investor losses.[42] As the U.S. Court of Appeals for the Second Circuit reminded the Commission in its 1997 ruling in *SEC v. Fischbach Corp.*, compensation of victims is "a distinctly secondary goal" of SEC actions.[43] The Fair Funds provision of the Sarbanes-Oxley Act of 2002 reflects a policy judgment that it is better for penalty money to go to injured investors than to the U.S. Treasury.[44] But it does *not* change the SEC's regulatory role or place it in the shoes of injured investors seeking compensation and should not be a reason to obtain a large penalty. Even in distributing the funds to harmed investors under Sarbanes-Oxley, normally the Commission itself does not determine who are the harmed investors but instead frequently asks the court to appoint an independent distribution consultant to make that judgment, subject to judicial review.

As former SEC Commissioner Cynthia Glassman concluded, we "cannot justify imposing penalties indirectly on shareholders whose investments have already lost value as a result of the fraud. Our use of so-called Fair Funds… leads to the anomalous result that we have shareholders paying corporate penalties that end up being returned to them through a Fair Fund—minus distribution expenses."[45] This is precisely the circularity problem which concerned Congress and which the SEC repeatedly promised to avoid in the exercise of its discretion.[46] Importantly, we do not question the value of compensating injured investors or the SEC's discretion to include in Fair Funds any penalties properly assessed against companies. But in such cases, the Remedies Act did not contemplate that the SEC's decision whether to seek penalties against a corporation—and in what amount—would be based "principally" on the "opportunity… of compensation for injured shareholders."

For the same reason, the Dodd-Frank Act should not affect the SEC's standards for whether to pursue corporate penalties and, if so, in what amounts. The new law introduces the risk that extraneous considerations will be perceived to drive more aggressive corporate penalties by the SEC to ensure funding for two new authorized recipients of collected penalties. The Act provides that:

1. In the event that information provided by a whistleblower leads to an enforcement action in which the SEC obtains monetary sanctions (including penalties, disgorgement and interest) exceeding $1 million, the SEC shall pay the whistleblower between 10% and 30% of the monetary sanctions imposed in the SEC action *and* in any "related actions" brought by the U.S. Attorney General, an appropriate regulatory authority, a self-regulatory organization, or a state attorney general in a criminal proceeding;[47] and

2. The Commission also may use the monetary sanctions it collects to fund activities of the SEC Inspector General set forth in the Act.[48]

Although the Dodd-Frank Act did touch on the penalty power and did establish these two new potential uses for the penalty money collected, it is telling that in doing so the legislation did not change the amount of each monetary threshold or the substantive standards defining the penalty tiers, as originally established under the Remedies Act. The Commission should not allow the increased number of potential beneficiaries of any collected penalties to impact the size of the corporate penalties it seeks.

Applying "Additional Factors"

The remaining seven factors in the 2006 framework—the so-called "additional factors"—accurately reflect various features of Congress's two core remedial objectives in the Remedies Act: *enhanced deterrence*, and flexibility for a *tailored remedy* to fit the seriousness of misconduct in each case. Of course, whether a corporate penalty is appropriate in a given case cannot be discerned by simple invocation of these broad goals. Accordingly, the Commission properly enumerated the host of specific interests contemplated by Congress—from the difficulty to detect or deter particular misconduct and the scale of complicity throughout a corporation; to the harm to innocent parties and the perpetrator's culpability.[49] These "additional considerations" offer guideposts for whether, given the misconduct in a particular case, the objectives of deterrence and a tailored remedy weigh in favor of a money penalty against the corporation. Yet equally relevant in each case—but insufficiently credited by the Commission in the past—are the 2006 framework's countervailing factors: the company's "*remedial steps*" and the company's "*cooperation* with Commission and other law enforcement."

Deterrence was the strongest rationale cited for the penalty power, whatever its merits as an empirical matter.[50] Congress authorized SEC penalties so the agency could change "the 'down-side' calculation for violations of the securities laws,"[51] otherwise a simple order of disgorgement or other injunctive relief leaves the defendant "no worse off than he would have been if he had chosen not to violate the law."[52] However, less powerful specific deterrence remedies are appropriate where the SEC detects violations within a company that had in place a reasonable system of compliance procedures and controls.[53] General deterrence interests are vindicated by such an enforcement approach—other companies will be encouraged to adopt similar procedures and controls reasonably designed to prevent violations of the securities laws.[54] The same is true as to the deterrence interests in redressing a company's unwillingness "to incur the cost of full compliance with the securities laws"[55] and in combating the "problem of recidivism."[56]

Congress and the SEC long have recognized that a company's efforts to prevent wrongdoing, its response upon detection of misconduct, and the subsequent degree of cooperation with any Staff investigation are crucial considerations to whether a monetary penalty is appropriate and, if so, the amount. Over the past decade, the SEC has repeatedly sought to strengthen its enforcement efforts through encouraging greater cooperation in its investigations.[57] In a 2001 Report of Investigation known as the "Seaboard Release," the Commission set forth standards for its determination "whether, and how much, to credit self-policing, self-reporting, remediation and cooperation—from the extraordinary step of taking no enforcement action to bringing reduced charges, *seeking lighter sanctions*, or including mitigating language in documents we use to announce and resolve enforcement actions."[58] Most recently, Enforcement Director Robert Khuzami underscored the Commission's commitment to promoting cooperation. Khuzami announced a "formal framework of incentives"—cooperation agreements, deferred prosecution agreements, and non-prosecution agreements based on "timely and necessary" assistance—as a potential "game-changer for the Enforcement Division."[59]

Thus, by the SEC's own terms, the degree of a corporation's voluntary remedial and cooperative efforts in aid of enforcement should materially shape the determinations whether to bring an action at all, whether fraud allegations are appropriate, and whether and, if so, how much of a penalty is appropriate. Essential to this enforcement initiative, however, is the provision of concrete, quantifiable benefits in return for cooperation. We do not suggest that *ex post* cooperation, alone, should preclude categorically a corporate penalty, but it should be an important factor to be considered. For the SEC to incentivize corporate measures to self-police, self-report, self-remedy and cooperate, the SEC must meaningfully and transparently credit remediation and cooperation in evaluating whether deterrence and tailored remedies necessitate a money penalty, or least a discounted one, against the corporation.[60]

As to the objective of tailored remedies, the scope of corporate compliance, remediation and cooperation informs the nature of the misconduct at stake. The SEC persuaded Congress that it needed "greater flexibility to tailor a remedy to the gravity of the violation,"[61] particularly in administrative proceedings against regulated entities that previously could be sanctioned only by either censure or revocation of firm registration. Explaining the SEC's remedial constraint "to deliver a pin-prick or to deliver the atom bomb," former SEC Chairman Breeden implored Congress to grant "some remedies in between."[62] Having secured the civil penalty remedy, the SEC now bears the responsibility to deploy it based on the nature of the misconduct in each case—informed, to be sure, by the level of intent or the scale of complicity in the corporation, but also by the degree of the corporation's compliance, remediation, and cooperation.

By providing in the Remedies Act a schedule of the permissible *sizes* of corporate money penalties, Congress left no doubt about the need for different remedial categories to reflect different levels of violations. The statute expressly tied the maximum authorized penalties to each of three tiers of misconduct:

- First tier: The violation does not involve second-tier or third-tier conduct.
- Second tier: The violation "involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement."
- Third tier: (i) The violation "involved fraud, deceit, manipulation, or deliberate or reckless disregard of a regulatory requirement"; *and* (ii) "such violation directly or indirectly resulted in substantial losses or created a significant risk of substantial losses to other persons."[63]

Under the statute, the maximum penalties courts may impose against corporations are, for a first-tier violation, the greater of $75,000 or "the gross amount of pecuniary gain to such defendant as a result of the violation" (intended to mean the amount of unjust enrichment);[64] for a second-tier violation, the greater of $375,000 or the amount of pecuniary gain; and for a third-tier violation, the greater of $725,000 or the amount of pecuniary gain.[65] The same penalty tiers and limits were prescribed for violations found in administrative proceedings, but without the alternative of higher penalties based on the amount of ill-gotten gains.[66]

These three tiers clearly reflect the congressional intent to calibrate penalties according to an ascending scale of the seriousness of the misconduct, measured by the level of intent exhibited by the violator, with possible further increases where the violator obtained a large amount of ill-gotten gains from the conduct. While the penalty amount can be increased through various theories of what constitutes a "violation" (with a separate penalty amount available for each "violation"), there is no reason to believe that Congress intended penalties in the tens or hundreds of millions of dollars to become commonplace.

Even a court's power to impose penalties equal to a corporation's pecuniary gain provides no more transparent or predictable grounding for some of the recent corporate penalties negotiated by the SEC in settled actions. Take, for instance, the financial fraud cases that have come to form a significant component of the SEC enforcement docket. In such cases, a corporation's theoretical gross pecuniary gain may be simply impossible to determine.[67] As one commentator observes, "the defendants' gain is difficult or impossible to calculate" following "fraudulent financial reporting, or negligent violations, such as incorrect books and records, failure to supervise, net capital deficiencies, or inaccurate periodic reports," for there is "no logical starting place for the calculation of a penalty."[68] Absent transparent grounding in the statutory penalty tiers and without a concrete basis to calculate the corporation's ill-gotten gain, there is a serious risk that the corporate penalties sought by the SEC instead will be perceived to be significantly impacted by political, media and public pressures for lofty figures.

Debate surely will persist, even concerning the appropriate tier within which to calculate each violation's fine, but recent penalties obtained by the SEC fail to reveal transparency, consistency or predictability based on identifiable criteria.

Part III: A New Paradigm for Use of the Corporate Civil Money Penalty Remedy

"The SEC now has the broadest range of remedies from which to choose and the greatest flexibility in applying these remedies than perhaps at any time in its history."[69] The Commission should return to a view of the monetary penalty as but one weapon in this broader remedial arsenal. As former Enforcement Director Lynch told Congress, "A civil money penalty should not become the *sine qua non* of all Commission enforcement actions."[70] A revised SEC corporate penalty framework should expressly consider the applicability of *nonpunitive* remedies at the Commission's disposal. Even prior to the passage of the Remedies Act, Senator Dodd underscored the SEC's "tremendous arsenal of enforcement powers, ranging from administrative sanctions to the ability to refer matters for criminal prosecution."[71]

Review of the history of the Remedies Act confirms that Congress clearly did not intend that the Commission use the penalty in all enforcement actions against public companies. Yet in major enforcement actions brought by the Commission in recent years, the sword of massive monetary penalties has been persistently dangled over corporations in settlement discussions. The Commission may well find that corporate penalties serve their policy goals more effectively if they are employed more selectively.

Indeed, as a practical matter, the most potent source of deterrence achieved by the Commission is not the economic cost imposed on a public company through massive penalties, but rather the reputational impact of an enforcement action brought by the Commission; that is, the public opprobrium faced by the corporation. Immediately accompanying the Commission's enforcement action against a public company are a bevy of negative news stories and adverse financial and other business consequences for that corporation. Even when a company settles an enforcement action without paying any penalty, the detailed recitation of fraud allegations set forth by the Commission in publicly filed documents can cause huge reputational damage and often spawns private litigation.

Even where the Commission deems a corporate penalty to be necessary, the deterrent effect may be achieved simply in the assessment of that penalty against the corporation, not in the inflated scale of such penalties. By its own account, the SEC does not determine the level of penalties with the objective to economically "hurt" the corporation, which would harm shareholders. In view of this prudent self-imposed limitation, the overall scale of penalties should be recalibrated substantially downward from the current levels to minimize the economic harm to shareholders while preserving the deterrent effect of the penalties.

Despite the public appeal of banner headlines announcing exorbitant penalties against public companies, it is crucial to the Commission's longstanding mission of investor protection that it make clear its focus remains only on remedial and not punitive relief. In reviewing its corporate penalty policy, the Commission should not confuse deterrence with retribution. The SEC was intended to be an impartial regulator, and it is most effective when it does not appear to be "taking sides"—regardless whether that partiality results from a goal of compensating investors or from perceived political, media, or public pressure.

NOTES

1. Statement of the Sec. & Exch. Comm'n Concerning Financial Penalties (Jan. 4, 2006), http://www.sec.gov/news/press/2006-4.htm.
2. Our sole focus is the SEC's standards for determining whether to seek money penalties against public companies. This article does not address the SEC decisions whether to seek penalties against individuals or the appropriate amount of such penalties, which raise different questions and considerations beyond the scope of our review here.
3. Kara Scannell, *SEC Taking Another Look at Penalty Policy*, THE WALL ST. J. (Mar. 6, 2010).
4. *See infra* notes 18, 47-48 and accompanying text.
5. In 1984 and 1988, Congress authorized the SEC to seek civil money penalties for insider trading violations, Insider Trading Sanctions Act of 1984, Pub. L. No. 98-376, 98 Stat. 1264 (codified in scattered sections of 15 U.S.C.A.); and Insider Trading and Securities Fraud Enforcement Act of 1988, Pub. L. No. 100-704, 102 Stat. 4677

(codified in scattered sections of 15 U.S.C.A.). In 1988, Congress authorized the SEC to seek civil money penalties for violations of the Foreign Corrupt Practices Act, Pub. L. No. 100-704, 102 Stat. 4677 (codified as amended at 15 U.S.C.A. § 78ff(c)(1)(B) (2006)).

6. Pub. L. No. 101-429, 104 Stat. 931 (amending the Securities Act of 1933, the Securities Exchange Act of 1934, the Investment Company Act of 1940, and the Investment Advisers Act of 1940).

7. *See* 15 U.S.C.A. § 77t(d) (2006); 15 U.S.C.A. § 78u(d)(3) (2006); 15 U.S.C.A. § 80a-41(e) (2006); 15 U.S.C.A. § 80b-9(e) (2006).

8. *See* 15 U.S.C.A. § 78u-2 (2006); 15 U.S.C.A. § 80a-9(d) (2006); and 15 U.S.C.A. § 80b-3(i) (2006).

9. *SEC v. Sony Corp.,* Case No. 1:98CV01935 (D.D.C) (filed Aug. 5, 1998), Litigation Release No. 15832, 67 S.E.C. Docket 1650, 1998 WL 439897 (S.E.C. Release No. 1998); *Securities and Exchange Commission Release Notice*, Litigation Release No. 16552, 72 S.E.C. Docket 1101, 2000 WL 576210 (S.E.C. Release No. 2000).

10. Xerox Settles SEC Enforcement Action Charging Company With Fraud; Xerox To Pay Largest Financial Fraud Penalty Ever Against Public Company; Company Agrees to Restatement of Financial Results, Special Review of Accounting Controls, SEC Press Rel. No. 2002-52 (Apr. 11, 2002), http://www.sec.gov/news/press/2002-52.txt. See generally *Report on the Current Enforcement Program of the Securities and Exchange Commission 27* nn. 98-102 and accompanying text (U.S. Chamber of Commerce, Mar. 2006).

11. Paul S. Atkins, Comm'r, U.S. Sec. & Exch. Comm'n, Remarks Before the U.S. Chamber Institute for Legal Reform (Feb. 16, 2006), http://www.sec.gov/news/speech/spch021606psa.htm. The consequences of corporate penalties for shareholders are particularly exorbitant where it is the standard practice for the SEC to insist the defendants "not seek to treat the civil penalties as tax deductible or eligible for reimbursement under their insurance policies." *See, e.g., SEC Fact Sheet on Global Analyst Research Settlements* (Apr. 28, 2003), http://www.sec.gov/news/speech/factsheet.htm.

12. *S.E.C. v. Worldcom, Inc.*, 273 F. Supp. 2d 431, 435-436, Fed. Sec. L. Rep. (CCH) P 92456 (S.D. N.Y. 2003).

13. Jan Larsen et al., *SEC Settlements; A New Era Post-SOX*, at 1 (NERA Economic Consulting, Nov. 10, 2008). The SEC has obtained a broad range of penalty amounts in recent settlements. *See, e.g., SEC v. Goldman, Sachs & Co. and Fabrice Tourre*, No. 10-CV-3229 (S.D.N.Y. July 14, 2010) (Consent of Defendant Goldman, Sachs & Co.), http://www.sec.gov/litigation/litreleases/2010/consent-pr2010-123.pdf ($535 million penalty); *SECURITIES AND EXCHANGE COMMISSION V. BANK OF AMERICA CORPORATION*, *CIVIL ACTION NOS. 09-6829, 10-0215 (S.D.N.Y)*, Litigation Release No. 21407, 2010 WL 421160 (S.E.C. Release No. 2010)($150 million penalty); *SECURITIES AND EXCHANGE COMMISSION V. DELL INC., MICHAEL S. DELL, KEVIN B. ROLLINS, JAMES M. SCHNEIDER, LESLIE L. JACKSON, NICHOLAS A.R. DUNNING*, *CIVIL ACTION NO. 1:10-CV-01245 (D.D.C.)*, Litigation Release No. 21599, Release No. 3156, Release No. AE - 3156, 2010 WL 2886401 (S.E.C. Release No. 2010) ($100 million); *SECURITIES AND EXCHANGE COMMISSION V. CITIGROUP INC.*, *CIVIL ACTION NO. 1:10-CV-01277 (ESH) (D.D.C. JULY 29, 2010)*, Litigation Release No. 21605, 2010 WL 2992476 (S.E.C. Release No. 2010)($75 million); *SEC V. DIEBOLD, INC., CIVIL ACTION NO. 1:10-CV-00908 (D.D.C.); SEC V. WALDEN ODELL, CIVIL ACTION NO. 1:10-CV-00909 (D.D.C.); AND SEC V. GREGORY GESWEIN, KEVIN KRAKORA, AND SANDRA MILLER*, *CIVIL ACTION NO. 5:10-CV-01235 (N.D. OHIO),* Litigation Release No. 21543, Release No. 3137, Release No. AE - 3137, 2010 WL 2199552 (S.E.C. Release No. 2010)($25 million penalty).

14. Barbara Black, Should the SEC be a Collection Agency for Defrauded Investors?, 63 BUS. LAW. 317, 328 (2008).

15. Statement of the Sec. & Exch. Comm'n Concerning Financial Penalties (Jan. 4, 2006), http://www.sec.gov/news/press/2006-4.htm.

16. Statement of the Sec. & Exch. Comm'n Concerning Financial Penalties (Jan. 4, 2006), http://www.sec.gov/news/press/2006-4.htm.

17. In 2007, SEC Chairman Christopher Cox announced that on a pilot basis, in some cases, the Enforcement Staff would be required to obtain the Commission's authorization before commencing settlement negotiations involving a monetary penalty. This changed the Staff's long-standing practice described above. *See* Theodore A. Levine & Wayne M. Carlin, *Implications of the New SEC Penalty Policy*, 38 BANK & CORP. GOVERNANCE L. REP. 636 (2007); Theodore A. Levine & Wayne M. Carlin, *Practical Implications of the SEC Pilot Penalty Policy*, 11 WALL ST. LAWYER 13 (2007). In 2009, however, SEC Chairman Mary Schapiro terminated this pilot program, allowing the Staff once again to negotiate and reach a proposed settlement with a prospective defendant before presenting it to the Commission for final approval. Mary L. Schapiro, Chairman, U.S. Sec. & Exch. Comm'n, Address to Practising Law Institute's "SEC Speaks in 2009" Program (Feb. 6, 2009), http://www.sec.gov/news/speech/2009/spch020609mls.htm.

18. *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 929P(a) (amending § 8A of Securities Act; § 21B(a) of Exchange Act; § 9(d)(1) of Investment Company Act; § 203(i)(1) of Investment Advisers Act). Historically, it was common for the SEC to bring a settled cease-and-desist proceeding and then, separately, to bring in federal court a settled action against the same party solely for purposes of obtaining a penalty that could not be obtained in the cease-and-desist proceeding.
19. The Securities Law Enforcement Remedies Act of 1989: Hearing on S. 647 Before the Subcomm. on Securities of the Comm. on Banking, Housing, & Urban Affairs, 101st Cong., 2d Sess., at 2 (Feb. 1, 1990) (statement of Sen. Christopher Dodd).
20. *See* U.S. Sec. & Exch. Comm'n, *Results of the Review of the Adequacy of Enforcement Remedies and Sanctions* 1, 7-8 (Feb. 22, 1984), *reprinted in SEC RESPONSES TO THE TREADWAY COMMISSION REPORT: A STUDY PREPARED FOR THE USE OF THE SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS OF THE COMMITTEE ON ENERGY AND COMMERCE*, 100th Cong., 2d Sess., at 137-150 (Exhibit H) (Comm. Print 1988).
21. U.S. Sec. & Exch. Comm'n, *Results of the Review of the Adequacy of Enforcement Remedies and Sanctions* at 7.
22. U.S. Sec. & Exch. Comm'n, *Results of the Review of the Adequacy of Enforcement Remedies and Sanctions* at 7-8.
23. By contrast with private suits for damages, the different requirements imposed by courts on the SEC in enforcement actions reflect its fundamentally remedial mission. For instance, in antifraud actions under § 10(b) of the Exchange Act, courts have imposed additional elements on private claimants not required of the SEC as plaintiff. *See, e.g., Geman v. S.E.C.*, 334 F.3d 1183, 1191, Fed. Sec. L. Rep. (CCH) P 92452 (10th Cir. 2003)(noting that unlike private actions under § 10(b), "[t]he SEC is not required to prove reliance or injury in enforcement actions").
24. Hearing Before the Subcomm. on Telecomm. and Fin. of the House Comm. on Energy and Commerce, at 22-23 (Sept. 17, 1987) (statement of David S. Ruder, Chairman, U.S. Sec. & Exch. Comm'n, Concerning Pending Legislation Regarding Contests for Corporate Control), *reprinted in* SEC RESPONSES TO THE TREADWAY COMMISSION REPORT, at 172-96 (Exhibit I). In 1987, a private commission on fraudulent financial reporting—the Treadway Commission—recommended that Congress provide the SEC with additional enforcement powers that included the authority to seek or to impose civil money penalties on those who violate federal reporting requirements. Congress already had extended this authority to the Commission to impose fines related to insider trading violations, *see supra* note 5, but for the vast variety of other securities law violations, including the general categories of fraud, the SEC could enjoin future violations of the securities laws and, when appropriate, obtain equitable remedies such as disgorgement.
25. Financial Reporting Practices (Part 2): Hearing Before the Subcomm. on Oversight and Investigations of the Comm. on Energy and Commerce, 100th Cong., 2d Sess., at 29 (May 2, 1988) (statement of David S. Ruder, Chairman, U.S. Sec. & Exch. Comm'n, Concerning the Recommendations of the National Commission on Fraudulent Financial Reporting) [hereinafter "Ruder Statement (1988)"].
26. Memorandum of the Securities and Exchange Commission in Support of the Securities Law Enforcement Remedies Act of 1989, at 4 (Apr. 1, 1988) [hereinafter "SEC Memorandum"], reprinted in Securities Law Enforcement: Hearing on H.R. 975 Before the Subcomm. on Telecomm. and Fin. of the Comm. on Energy and Commerce, 101st Cong., 1st Sess., at 44-59 (July 19, 1989) (statement of David S. Ruder, Chairman, U.S. Sec. & Exch. Comm'n, Attachment A).
27. SEC Memorandum at 4.
28. SEC Memorandum at 5 (emphasis added).
29. SEC Memorandum at 4 (footnote omitted).
30. SEC Memorandum at 4-5.
31. The Securities Law Enforcement Remedies Act of 1989: Hearing on S. 647 Before the Subcomm. on Securities of the Comm. on Banking, Housing, & Urban Affairs, 101st Cong., 2d Sess., at 44-45 (Feb. 1, 1990) (statement of Richard C. Breeden, Chairman, U.S. Sec. & Exch. Comm'n) [hereinafter "Breeden Statement"].
32. The Securities Law Enforcement Remedies Act of 1989: Hearing on S. 647 Before the Subcomm. on Securities of the Comm. on Banking, Housing, & Urban Affairs, 101st Cong., 2d Sess., at 116 (Feb. 1, 1990) (statement of Gary G. Lynch, Former Dir. of Enforcement, U.S. Sec. & Exch. Comm'n) [hereinafter "Lynch Statement"].
33. Lynch Statement at 121.
34. Lynch Statement at 128-129.
35. Lynch Statement at 131.
36. S. REP. No. 101-337, at 17 (1990) (emphasis added).
37. H.R. REP. No. 101-616, at 18-19 (1990); *see also* S. REP. No. 101-337, at 11-12 (1990).

38. Statement of the Sec. & Exch. Comm'n Concerning Financial Penalties (Jan. 4, 2006), http://www.sec.gov/news/press/2006-4.htm.
39. SEC Memorandum at 4.
40. *See, e.g.*, Linda Chatman Thomsen, Dir. of Enforcement, U.S. Sec. & Exch. Comm'n, Statement Regarding McAfee, Inc. and Applix, Inc. (Jan. 4, 2006), http://www.sec.gov/news/speech/spch010406lct.htm. *See also SECURITIES AND EXCHANGE COMMISSION V. MCAFEE, INC., CIVIL ACTION NO. 06-009 (PJH) (N.D. CAL.) (JANUARY 4, 2006) SEC SUES MCAFEE, INC. FOR ACCOUNTING FRAUD MCAFEE AGREES TO SETTLE AND PAY A $50 MILLION PENALTY*, Litigation Release No. 19520, Release No. 2360, Release No. AE—2360, 87 S.E.C. Docket 169, 2006 WL 20378 (S.E.C. Release No. 2006); *IN THE MATTER OF APPLIX, INC., RESPONDENT.*, Release No. 33, 8651, Release No. 34, 53049, Release No. 2359, Release No. 8651, Release No. 53049, Release No. AE—2359, 87 S.E.C. Docket 103, 2006 WL 20379 (S.E.C. Release No. 2006).
41. S. REP. No. 101-337, at 17 (1990) .
42. *See, e.g.*, Theodore A. Levine & Patricia J. Thompson, *An Unwarranted Expansion of Authority*, THE CORP. & SEC. LAW ADVISOR 12, 21 (July 1989); Black, *supra* note 14.
43. *S.E.C. v. Fischbach Corp.*, 133 F.3d 170, 175, Fed. Sec. L. Rep. (CCH) P 90101 (2d Cir. 1997). Congress even pointedly distinguished the remedies of disgorgement and compensation, as the House Report stated: "In contrast to damages granted in private actions, which are designed to compensate the victims of a violation, disgorgement 'is a method of forcing a defendant to give up the amount by which he was unjustly enriched.'" H.R. REP. NO. 101-616, at 22 (1990) (quoting *S.E.C. v. Blavin*, 760 F.2d 706, 713 (6th Cir. 1985)). *See also supra* note 23 (noting different requirements in private actions and SEC actions).
44. *See* Pub. L. No. 107-204, § 308, 116 Stat. 745 (codified as amended at 15 U.S.C.A. § 7246 (2006)) (authorizing money penalties to be directed, at the SEC's discretion, to victims of the securities law violations, instead of channeling it to the U.S. Treasury). Nothing in the SOX statute or its legislative history altered the terms on which the SEC may secure money penalties.
45. Cynthia A. Glassman, Comm'r, U.S. Sec. & Exch. Comm'n, "SEC in Transition: What We've Done and What's Ahead" (June 15, 2005), http://www.sec.gov/news/speech/spch061505cag.htm. In similar terms, former SEC Commissioner Joseph Grundfest has explained, "In at least some cases, there's the perspective that these fines punish the victims twice." *See* Alix Stuart, *Penalty Box*, CFO MAGAZINE, Feb. 1, 2006, at 81.
46. Verity Winship, *Fair Funds and the SEC's Compensation of Injured Investors*, 60 FLA. L. REV. 1103, 1128 (2008). ("When a corporation pays compensation, the current shareholders indirectly bear the costs; the compensation goes to holders of shares within the time period in which [the violation] allegedly affected the market. Accordingly, compensation in these circumstances amounts to a wealth transfer between shareholders, none of whom is culpable. Furthermore, diversified investors may both receive and pay compensation because they are current shareholders (paying the penalty) and also were shareholders during the relevant period (receiving compensation, minus administrative costs).").
47. *See* Dodd-Frank Act § 922(a) (inserting in the Exchange Act § 21F: Securities Whistleblower Incentives and Protection). *See generally* Theodore A. Levine, John F. Savarese & Wayne M. Carlin, *A New World for Whistleblowers Under the Dodd-Frank Legislation,* 45 Bank & Corp. Governance L. Rep. 51 (2010).
48. *See* Dodd-Frank Act § 966 (inserting in Exchange Act § 4D: Additional Duties of Inspector General).
49. These considerations also recall six factors set forth in the Remedies Act for the Commission to consider in administrative proceedings in determining whether to impose a monetary penalty "in the public interest": (1) whether the violation involved fraud, deceit, manipulation or deliberate or reckless disregard of a regulatory requirement; (2) harm to others caused by the violation; (3) the amount of unjust enrichment, taking into account any restitution made to persons injured by the violation; (4) whether the person was found by the Commission or other appropriate regulatory body to have previously committed a violation of the securities laws or to have previously been enjoined from committing such violations; (5) the need to deter such persons or others from committing such violations; and (6) "such other matters as justice may require." *See* Exchange Act § 21B(c), 15 U.S.C.A. § 78u-2(c) (2006).
50. It is questionable whether the scale of a penalty affects the level of corporate deterrence. As one scholar observed, "Very broadly, it is the certainty of punishment rather than its severity which has a deterrent effect." M. PHILIP FELDMAN, CRIMINAL BEHAVIOUR: A PSYCHOLOGICAL ANALYSIS 214 (1977). *See also infra* Part III.
51. Breeden Statement at 53.
52. Breeden Statement at 41.

53. As the federal appeals court explained in one decision striking down SEC punitive sanctions as excessive, "Although the SEC's opinion references these [appropriate] factors, the opinion does not reflect that the SEC meaningfully considered these factors when it imposed the sanctions.... [T]he conduct was not particularly egregious; ... the [violation was]... a fairly isolated occurrence and... the likelihood of a future violation is slight.... [Defendant] voluntarily [took steps]... making the possibility of a future violation more remote." *Monetta Financial Services, Inc. v. S.E.C.*, 390 F.3d 952, 957-958, Fed. Sec. L. Rep. (CCH) P 93041 (7th Cir. 2004). *Cf. WHX Corp. v. S.E.C.*, 362 F.3d 854, 855, Fed. Sec. L. Rep. (CCH) P 92731 (D.C. Cir. 2004)(invalidating as arbitrary and capricious, given the record in the case, the SEC's remedial decision to issue a cease-and-desist order).

54. *See, e.g., IN THE MATTER OF BEAR, STEARNS & CO. INC.; CITIGROUP GLOBAL MARKETS, INC.; GOLDMAN, SACHS & CO.; J.P. MORGAN SECURITIES, INC.; LEHMAN BROTHERS INC.; MERRILL LYNCH, PIERCE, FENNER & SMITH INCORPORATED; MORGAN STANLEY & CO. INCORPORATED AND MORGAN STANLEY DW INC.; RBC DAIN RAUSCHER INC.; BANC OF AMERICA SECURITIES LLC; A.G. EDWARDS & SONS, INC.; MORGAN KEEGAN & COMPANY, INC.; PIPER JAFFRAY & CO.; SUNTRUST CAPITAL MARKETS INC.; AND WACHOVIA CAPITAL MARKETS, LLC*,, Release No. 33, 8684, Release No. 34, 53888, Release No. 8684, Release No. 53888, 88 S.E.C. Docket 259, 2006 WL 1490228, *7 (S.E.C. Release No. 2006)("While all Respondents cooperated with the Commission, Banc of America Securities will be assessed a *lesser civil monetary penalty because of the quality of its self-monitoring capabilities* in the auction rate securities area that it demonstrated to the Commission staff.") (emphasis added).

55. Breeden Statement at 42; *see also* Breeden Statement at 44-45 (testifying that where noncompliance "involves isolated or unintentional conduct, the implementation of new procedures or a similar remedial measure will often be the most appropriate resolution of the case").

56. Securities Law Enforcement: Hearing on H.R. 975 Before the Subcomm. on Telecomm. and Fin. of the Comm. on Energy and Commerce, 101st Congress, 1st Session, at 31 (July 19, 1989) (statement of David S. Ruder, Chairman, U.S. Sec. & Exch. Comm'n) [hereinafter "Ruder Statement (1989)"]; Breeden Statement at 43; *see also* The Securities Law Enforcement Remedies Act of 1989: Hearing on S. 647 Before the Subcomm. on Securities of the Comm. on Banking, Housing, & Urban Affairs, 101st Cong., 2d Sess., at 90-91 (Feb. 1, 1990) (testimony of Aulana L. Peters, Former Comm'r, U.S. Sec. & Exch. Comm'n).

57. *See* Wayne M. Carlin & David B. Anders, *SEC Cooperation Initiatives*, 44 BANK & CORP. GOVERNANCE L. REP. 39 (2010).

58. Report of Investigation Pursuant to § 21(a) of the Securities Exchange Act of 1934 and Comm'n Statement on the Relationship of Cooperation to Agency Enforcement Decisions, SEC Rel. No. 44969, SEC Rel. No. AE-1470, Oct. 23, 2001 ("Seaboard Release") (emphasis added).

59. Robert S. Khuzami, Dir. of Enforcement, U.S. Securities & Exchange Comm'n, Remarks at News Conference Announcing Enforcement Cooperation Initiative and New Senior Leaders (Jan. 13, 2010), http://www.sec.gov/news/speech/2010/spch011310rsk.htm; *see also* U.S. Sec. & Exch. Comm'n Div. of Enforcement, Enforcement Manual § 6: Fostering Cooperation (Jan. 13, 2010). In the United Kingdom, too, the Financial Services Authority expressly adopted as one factor in determining appropriate sanctions "how cooperative the firm or individual is," from self-reporting and self-investigation to self-remediation and cooperation with law enforcement authorities. *See* Financial Services Authority: The Benefits to Firms and Individuals of Cooperating with the FSA, http://www.fsa.gov.uk/Pages/doing/regulated/law/focus/co-operating.shtml (setting forth relevant indicia of corporate cooperation).

60. The FSA's recent settled action that included an expressly discounted penalty against J.P. Morgan Securities Ltd. illustrates some degree of transparency in applying credit for cooperation. The FSA stated: "In working out the level of the penalty the FSA took into account that the misconduct was not deliberate and that the firm self-reported on discovering the issue—it also immediately remedied the situation.... The firm worked constructively with the FSA in the course of its investigation and agreed to settle at an early stage. In doing so it qualified for a 30% discount." *FSA Levies Largest Ever Fine of £33.32m on J.P. Morgan Securities Ltd. for Client Money Breaches* (June 3, 2010), http://www.fsa.gov.uk/pages/Library/Communication/PR/2010/089.shtml. For cases in which the SEC reached settlements with substantially reduced civil penalties against a broker-dealer based on their agreement to cooperate, *see, e.g., SEC v. Cutillo et al.*, No. 09 Civ. 9208 (S.D.N.Y. Mar. 30, 2010); *SEC v. Galleon Mgmt., LP et al.*, No. 09 Civ. 8811 (S.D.N.Y. Apr. 19, 2010). *See* Theodore A.

Levine, Wayne M. Carlin & Kevin S. Schwartz, *SEC Agrees to Reduce Penalties in Exchange for Cooperation*, 44 BANK & CORP. GOVERNANCE L. REP. 655 (2010). Moreover, the assignment of no penalty should be a real and available point on the spectrum, not merely a theoretical point reached only in the most extraordinary cases.

61. Ruder Statement (1989) at 25; *see also* Breeden Statement at 32, 43-44.
62. Breeden Statement at 32; *see also* Ruder Statement (1989) at 69.
63. *See* 15 U.S.C.A. § 77t(d)(2) (2006); 15 U.S.C.A. § 78u(d)(3) (2006); 15 U.S.C.A. § 80a-41(e)(2) (2006); 15 U.S.C.A. § 80b-9(e)(2) (2006).
64. The statute does not use the term "unjust enrichment," but rather refers to "the gross amount of pecuniary gain" to the defendant as a result of the violation, which the Senate Report confirms to mean "the amount by which the defendant was unjustly enriched," S. REP. No. 101-337, at 13 (1990), typically the amount of disgorgement.
65. These figures reflect the penalties prescribed in the Remedies Act as adjusted, by regulation, for inflation. 17 C.F.R. § 201.1004 (Supp. 2010).
66. *See* 15 U.S.C.A. § 78u-2(b) (2006); 15 U.S.C.A. § 80a-9(d)(2) (2006); 15 U.S.C.A. § 80b-3(i)(2) (2006).
67. *See generally* Black, *supra* note 14, at 321-322 nn.26-28 and accompanying text (noting that in cases of misstatements by a corporation not selling its securities, the SEC sought disgorgement from corporate insiders who profited from trading in the company's securities during the period of misinformation *but* "did not seek disgorgement from entity defendants… because while the entity may have benefited in many ways from its increased market capitalization, it is hard to identify any 'profits' or 'ill-gotten gains' in the absence of the entity's sale of its securities"); Black, *supra* note 14, at 329 ("A corporate defendant… does not experience what has traditionally been considered ill-gotten gains in the absence of sales of its own securities.").
68. Arthur B. Laby & W. Hardy Callcott, Patterns of SEC Enforcement Under the 1990 Remedies Act: Civil Money Penalties, 58 ALB. L. REV. 5, 49-50 (1994).
69. Theodore A. Levine & Daniel M. Hawke, *Sarbanes-Oxley: Back to the Future*, CHIEF LEGAL EXECUTIVE 14, 15 (2003).
70. Lynch Statement at 121.
71. The Securities Law Enforcement Remedies Act of 1989: Hearing on S. 647 Before the Subcomm. on Securities of the Comm. on Banking, Housing, & Urban Affairs, 101st Cong., 2d Sess., at 2 (Feb. 1, 1990) (statement of Sen. Christopher Dodd).