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Should the SEC Be a "Tough Cop"?

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On September 26, SEC Chair Mary Jo White delivered her first public speech setting forth her vision for the SEC's enforcement program. She took the opportunity to highlight some areas of emphasis in her efforts to strengthen the SEC's function and image as a "tough cop". We support a vigorous and fair SEC enforcement program, and we have used the policeman analogy ourselves from time to time. But in the current atmosphere, that analogy may encourage some significant misconceptions about the SEC's role.

In large part, Chair White's remarks reflect a continuation and intensification of a trend that began under her predecessor—the effort to import into the SEC some of the tools and the mindset of criminal prosecutors. In a time when the SEC is under attack by the press and politicians for not being tough enough, it can be easy to forget that the SEC is principally a regulatory agency, and that it is not in the business of meting out punishment. As a regulator, the SEC's only enforcement function is remedial—to shine a light on and improve business conduct, protect investors and markets, and deter future misconduct. Historically, the SEC has been most effective when it has kept its focus on performing that regulatory function.

The distinction between these two perspectives on the SEC's role plays out, for example, in the SEC's use of associational bars. Chair White rightly identified this power

as one of the SEC's "most potent" tools. But while these bars may feel like punishment to the individuals who receive them, they are not punitive measures. They are instead remedial forms of relief designed to remove a wrongdoer from a position in which he or she could cause future harm to investors (predicated upon a showing that there is a risk of such future harm). The SEC employs these measures when it concludes, based on findings of misconduct, that a registered representative should no longer be in a position of selling securities to investors, a corporate officer or director should no longer be entrusted with the responsibilities of those positions, or an accountant or lawyer should no longer be permitted to practice as a professional before the SEC. In each case, the bar is a protective, forward-looking regulatory action. It is not retribution.

Another recent theme is reflected in Chair White's observation that, under current law, the SEC cannot assess civil money penalties "based on investor losses." The SEC's mandate—again as a regulator—should not entail stepping into the shoes of investors in order to seek compensation for their losses. Enforcement actions sometimes do result in compensation flowing to investors, but that is a consequence of the regulatory process, not its *raison d'etre*. Turning the civil-penalty power into a mechanism for investor compensation further distorts the regulatory enforcement process by introducing an outcome-driven perspective that is inconsistent with a fair-minded consideration of the question whether or not anyone in fact violated the law.

Chair White made clear that the SEC's heightened emphasis on bringing charges against individuals will continue. Indeed, she commented that she wants the SEC to be "looking first at the individual conduct and working out to the entity." She called this a shift that "could bring more individuals into enforcement cases." It is unclear what this will ultimately mean for the conduct of investigations in the corporate context. SEC investigations—whether they involve accounting improprieties, disclosure problems, FCPA violations or other issues—generally focus on events that were the result of conduct by multiple individuals. In our experience, the SEC's investigative approach, at its best, has been to develop a full investigative record and then to assess in an even-handed manner whether any entities *or individuals* acted with a degree of culpability that warrants enforcement action. As Chair White noted, the SEC frequently does bring charges against individuals. But when the evidence does not warrant such charges, the SEC rightly determines not to pursue them. The SEC's principled exercise of judgment in those cases deserves praise, not external pressure to do otherwise.

Chair White also spoke about the SEC's departure from its decades-long practice of settling all cases on a no admission or denial basis, a policy that has served the SEC well

throughout its history. She identified the following types of cases in which the Commission may seek admissions of wrongdoing as a condition of settlement:

- Cases where a large number of investors have been harmed or the conduct was otherwise egregious.
- Cases where the conduct posed a significant risk to the market or investors.
- Cases where admissions would aid investors deciding whether to deal with a particular party in the future.
- Cases where reciting unambiguous facts would send an important message to the market about a particular case.

While it is always helpful to know the criteria the SEC will apply in administering its enforcement program, these factors provide only limited insight. Though Chair White expressed the view that settling cases *without* seeking any admissions "makes very good sense" in "most" cases, her use of terms such as "otherwise egregious" and "send[ing] an important message" leaves the staff and Commission with a tremendous measure of subjective discretion. Only time and experience will tell us how the SEC will deploy its new admissions weapon. The two settlements in which the SEC has so far obtained admissions were sufficiently dissimilar as to yield little clear insight on this score. If demands for admissions become a commonplace condition of settlement, rather than the rare exception, the SEC's regulatory enforcement program will be weakened rather than strengthened.

We do not start—as many commentators and observers do—from a perspective that the SEC's enforcement program is anemic and faltering. To the contrary, it is robust and aggressive, with many formidable tools already at its disposal. Of course, even the best government program can always be improved. It is our hope that the SEC will keep its eye on its regulatory role in charting the future course of its enforcement program.

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