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Highlights from SEC Speaks 2024

Chair/Commissioner Remarks and Litigation and Enforcement Trends

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The U.S. Securities and Exchange Commission (the "SEC") held its annual SEC Speaks conference—after a hiatus in 2023—on April 3 and 4, 2024 in Washington, D.C. The conference featured remarks from Chair Gary Gensler, Commissioner Hester Peirce, Commissioner Mark T. Uyeda, and Director of the Division of Enforcement (the "Division") Gurbir S. Grewal, as well as panel discussions addressing current SEC initiatives, priorities, and enforcement trends for the upcoming year. The conference speakers and panels also provided an update on litigation, judicial, and legislative developments.

The panels emphasized the SEC's three-fold mission of (i) protecting investors; (ii) maintaining fair, orderly, and efficient markets, and (iii) facilitating capital formation.

Highlights from this year's conference included significant discussion of the treatment of cryptocurrency assets; the SEC's focus on individual accountability, self-reporting and cooperation considerations; the SEC's active whistleblower program; and other enforcement and examination trends from the past year.

Chair's Speech and Commissioners' Remarks

Statement of Chair Gensler

Chair Gary Gensler started the SEC Speaks conference by recounting the history of the securities laws from their enactment under President Franklin D. Roosevelt, to later amendments under President Gerald Ford in the 1970s, and including continued reforms well into today. In doing so, he observed that the SEC, as it has done for 90 years, "will continue to update the rules of the road for investors and issuers alike." Chair Gensler centered his remarks on the importance of "two key public goods: first, instilling greater trust, and second, instilling greater efficiency and competition in the capital markets."

In discussing clearinghouses and settlements, Chair Gensler remarked that clearinghouses are vital to our markets because they serve as the "plumbing" for the market. He stated that, on May 28, 2024, Commission rule "T+1" will go into effect, which will shorten the settlement cycle to one business day in order to facilitate more competitive trading. Chair Gensler noted that the SEC also adopted rules in December 2023 to expedite central clearing for U.S. Treasury markets, by making "changes to enhance customer clearing" and by "broaden[ing] the scope of which transactions clearinghouses must clear." Chair Gensler stated that "[e]nhanced access to central clearing can facilitate all-to-all trading, competition, and resiliency in these markets. These rules help fulfill Congress's mandates to promote efficiency, competition, liquidity, and resiliency in the markets."

Chair Gensler also discussed broker-dealers' execution duties, noting that he has "long considered broker-dealers' best execution duty to their customers to be critical to both trust and competition in the markets." Accordingly, he observed that, when he joined the SEC in 2021, he was "surprised to learn" that "the Commission actually didn't have its own best execution rule." For this reason, Chair Gensler noted that he believed that "a best execution standard is too central to the SEC's mandate to protect investors, not to have on the books as a Commission rule. Rapid developments in our markets

make best execution that much more important."

Statement of Commissioner Peirce

Commissioner Hester M. Peirce delivered her remarks, "At the SEC: Nothing but Crickets," by referencing her previous statement from a the SEC Speaks conference in 2019 where she had noted that the SEC had a "secret garden," or a "maze of staff guidance that serves to define practices across the securities industry in a way that may be inconsistent with a plain reading of the rulebook." Commissioner Peirce stated that this "secret garden" of guidance "is not promulgated through notice-and-comment rulemaking, but appears in staff statements and speeches, phone calls, some types of no-action letters, and the like."

Commissioner Peirce stated that Staff Accounting Bulletin ("SAB") 121—which requires that public companies holding crypto assets for clients put a liability and corresponding asset on their balance sheets reflecting the value of the crypto asset—was a "pernicious weed" that sprang up since her last address. She noted that, in her view, SAB 121 "was issued apparently without input from the public or banking regulators, who subsequently have expressed concerns." Commissioner Peirce stated that the Government Accountability Office ruled last October that SAB 121 should have been submitted to Congress for its review under the Congressional Review Act.

Additionally, Commissioner Peirce criticized the SEC's practice of rulemaking based on what she described as "the dwindling of genuine Commission and staff engagement with the public." She stated that "[t]he Commission—not the staff or market participants—is to blame." Commissioner Peirce stated that the comment period should be used to foster discussion and the Commission should not force the public to adapt to unworkable rules. She stated that the Commission should thoughtfully seek more public involvement.

Commissioner Peirce likewise shared her observations on engagement with the SEC staff, stating that "[p]roductive interactions with the SEC are fewer and further between than they were in the past." Specifically, she stated that "[t]he stilted communication, half-hearted engagement, quick-draw of enforcement guns, and limited transparency that characterize the Commission's current relationship with the industry we regulate should concern anyone who cares about this great institution and the amazing markets we regulate."

Commissioner Peirce outlined several steps she believed that the SEC should take to encourage public engagement, including the following:

- Paring back to the Commission's rulemakings;
- Working with the public to identify problems and tailor solutions;
- Proposing realistic rules without "clickbait" provisions;
- Forming an advisory committee made of chief compliance officers;
- Providing greater insight into registration statement application and review;
- Identifying and articulating issues delaying Commission action and creating plans to resolve them; and
- Encouraging staff to work through challenging regulatory issues, including both how the implementation of new technologies might hurt investors and how blocking the implementation of new technologies may hurt investors.

Statement of Commissioner Uyeda

In his statement, Commissioner Mark T. Uyeda emphasized that the SEC's reputation for excellence depends on its ability to adhere to its mission, which, according to Commissioner Uyeda, cannot be taken for granted. He explained the Commission must remain "focused on its narrow mission, even when political activists would seek to transform the agency's authority to achieve policy objectives that are outside of [the Commission's] statutory mandate."

Commissioner Uyeda discussed the Commission's recent Climate Rule, which he noted requires issuers to disclose certain climate-related information. Commissioner Uyeda outlined the Climate Rule as requiring a company to disclose certain climate risks; a company's consideration, oversight, and plans for climate risks; and the financial impact of climate risks in a company's financial statements. He noted that recent amendments to the Climate Rule are "designed to alter the behavior of public companies in a manner that serves political interests that have otherwise failed to achieve such change through the legislative process."

Commissioner Uyeda further stated that the Climate Rule's "fundamental flaw is that it mandates disclosures not financially material to investors." Commissioner Uyeda described the Climate Rule as an attempt by the Commission to retreat from materiality in order to advance a different agenda of broad policy and economic goals. He characterized such agenda as

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"veer[ing] far beyond the Commission's jurisdiction."

Commissioner Uyeda noted that the SEC's conflict mineral disclosure rule, which requires public disclosure of use of certain conflict materials in the Democratic Republic of Congo, provides an illustrative example of the challenges that the Climate Rule may face. He noted that, while the conflict mineral rule was adopted (following a congressional mandate) to achieve a social purpose, it, in effect and in Commissioner Uyeda's view, imposed a mandatory disclosure rule on public companies that deviated from the financially material standard. He explained the effectiveness of the rule was impaired by the post-adoption high demand of materials that were not required to be disclosed by the conflict mineral rule. Commissioner Uyeda used this example to illustrate the evolving nature of social and policy issues.

Statement of Director Grewal

In his remarks, Director Gurbir S. Grewal advised that the Division is "facing significant headwinds in our enforcement efforts." In discussing crypto enforcement, Director Grewal indicated that the Division's approach has been "consistent, principled, and tethered to the federal securities laws and legal precedent." He reiterated that the applicable test to determine whether a crypto asset is a security is the *Howey* test. He stated that the Division has clearly and consistently applied (over the past decade) the *Howey* analytical framework to protect investors in the crypto space, but the SEC has seen significant non-compliance, with many questioning the Division's jurisdiction and advancing "creative attempts" to avoid enforcement. According to Director Grewal, the Division has faced "[a] decade's worth of arguments that have served as nothing more than a distraction from the very real issues and risks that the crypto markets present for the investing public."

Director Grewal further stated the crypto enforcement actions have been among the hardest fought in his entire career and indicated the Division will continue the fight because "investor protection demands it." He noted that, given the non-compliance in the crypto space, the investing public has "good reason to be concerned."

Director Grewal noted the sentencing of Samuel Bankman-Fried and the hundreds of victim statements submitted in advance of the sentencing, which reflected the broad cross-section of people who were harmed by Bankman-Fried's fraud. Director Grewal also offered additional examples of enforcement actions that, according to Director Grewal, highlight "predatory inclusion" tactics that certain crypto entities are directing at marginalized communities.

Director Grewal then specifically addressed a "headwind" that the SEC faces from certain market participants: "attacks on [the Commission's] integrity." He emphasized that the SEC does not act for financial incentives or for personal gain; nor does the SEC round corners in order to prevail. Instead, Director Grewal stated, a majority of the Enforcement Division does it for one reason alone: "standing up each and every day for the investing public." He emphasized that the public must have confidence and trust that the SEC "will hold bad actors accountable when they violate the securities laws regardless of who, or how powerful, they are."

Division of Enforcement

The conference also included multiple panels featuring members of the Enforcement Division, touching on priorities and highlights from across a wide range of enforcement areas.

Enforcement Statistics and Initiatives

Sanjay Wadhwa, Deputy Director of the Division of Enforcement, highlighted the SEC's work over the prior fiscal year. Specifically, he reported that, in Fiscal Year 2023, the SEC filed 784 total enforcement actions, which was a three-percent increase over the prior fiscal year. In addition, Mr. Wadhwa noted that this figure included 501 original or standalone enforcement action, which constituted an eight-percent increase over the past fiscal year. Furthermore, he said that the SEC obtained just under $5 billion in financial remedies during the last fiscal year, which was the second highest amount in SEC history after the record-setting year in fiscal year 2022. The breakdown of financial remedies was approximately $3.37 billion in disgorgement and prejudgment interest and almost $1.6 billion in civil penalties. Notably, the SEC obtained orders barring 133 individuals from serving as officers and directors of public companies, which was the highest number of officer and director bars obtained in a decade.

Mr. Wadhwa noted that fiscal year 2023 was a "record-breaking" year for the SEC's Whistleblower Program, as the SEC issued whistleblower awards totaling nearly $600 million, the most ever awarded in one year. This included a record-breaking $279 million awarded to one whistleblower. Further, the Whistleblower Program received more than 18,000 tips during fiscal year 2023, nearly 50% more than the prior record set in fiscal year 2022.

Additionally, Mr. Wadhwa discussed two ongoing enforcement initiatives: the record-keeping and amended marketing

material initiatives. First, Mr. Wadhwa explained the Division has charged nearly 60 firms (investment advisers, broker-dealers, and credit ratings agencies) with record-keeping violations since December 2021. As a result, according to Mr. Wadhwa, the Division has been criticized with respect to its assessment of civil penalties in these types of matters. In response to such criticism, Mr. Wadhwa noted that the SEC conducts an individualized assessment of each firm, based on a number of factors, including: the firm's size, the revenues from the regulated parts of the firm's business, the scope of the firm's violations, precedent, the firm's self-reporting efforts, and the firm's cooperation with the SEC. He noted the most important factor with respect to reducing civil penalties is self-reporting. Mr. Wadhwa emphasized that civil penalties must be adequate to ensure deterrence.

Second, Mr. Wadhwa discussed the amended marketing initiative and related enforcement actions. According to Mr. Wadhwa, the SEC reviews a number of factors with respect to this initiative, including the firm's regulated assets under management, regulatory history, remedial measures, self-reporting efforts, and cooperation with the SEC. Mr. Wadhwa emphasized that none of these factors is dispositive, and that the Division considers each factor with its recommendations to the Commission. Finally, he noted that all of these "factors are almost certainly going to be relevant in any SEC investigation you may be dealing with."

Individual Accountability

Stacy Bogert, Associate Director of the Division of Enforcement, discussed the Division's focus on holding individuals accountable. Ms. Bogert stated the Division is very "conscious" of the remedies it seeks in order to deter future individual violations from reoccurring or repeating. Such remedies, she stated, include disgorgement and clawbacks of executive compensation in certain circumstances under Section 304 of the Sarbanes-Oxley Act of 2002 ("SOX 304"). Mr. Bogert noted that SOX 304 clawbacks are not limited to the fraud delta and that SOX 304 applies, even if the chief executive officer or chief financial officer were not involved in the relevant conduct. Ms. Bogert also highlighted other relief used to protect the investing public from future violations and the integrity of the markets, including injunctions and officer and director bars. Ms. Bogert noted that injunctions can be tailored to prevent individual participation in offerings, marketing and association within certain markets and programs, citing, as an example, the crypto market. Ms. Bogert pivoted to noting that, during fiscal year 2023, the SEC secured the highest amount of bar orders in over a decade. She explained that officer and director bars will continue to be a key part in the relief that the SEC seeks.

Entity Accountability

Charlotte Buford, Deputy Chief Counsel of the Division of Enforcement, spoke on a wide-range of topics related to entities, including accountability, gatekeeping accountability and civil penalties. Ms. Buford emphasized the importance of not only looking at past conduct to hold entities accountable, but also of future conduct in order to deter future violations. She reiterated that financial remedies play an important role in entity accountability and, if available, provide an avenue to distribute back to investors. Ms. Buford explained, however, that non-financial relief has an important role, too. As an example, she noted that the SEC may require independent compliance consultants to evaluate company policies and procedures in order to ensure correct procedures are developed and implemented. Ms. Buford explained that the SEC's goals are to protect investors going forward and to prevent reoccurrence of any institutional or corporate failures or violations on the part of entities. She concluded by explaining that the corporate remedies the SEC seek encourage self-reporting, cooperation and other remedial actions.

Importance of Gatekeepers

Ryan Wolfe, Enforcement Chief Accountant, addressed the role of gatekeepers. Mr. Wolfe identified three types of gatekeepers: (i) preparers, which include chief executive officers, accountants, and others who create financial statements that are distributed to investors; (ii) auditors and assurance providers; and (iii) individuals who are in charge of corporate governance, which include board directors. Mr. Wolfe explained that accountants and other gatekeepers are integral to capital markets and market integrity, and as such, must be held accountable. Mr. Wolfe noted that gatekeepers have accepted professional responsibilities and must adhere to those accepted responsibilities. Mr. Wolfe noted that accountability is integral to creating an environment that protects investors and creates trust in the markets. As a final thought, he explained that it is not only about the "gatekeepers" but also about the "gates." The "gates," or the controls and systems, Mr. Wolfe stated, must protect investors by detecting and correcting misstatements before such statements are disseminated to investors.

Importance of Cooperation

Samuel Waldon, Chief Counsel for the Division of Enforcement, focused his discussion on the topic of cooperation by those subject to investigations. He discussed the importance of timing with respect to cooperation, noting that the earlier,

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the better and that an entity or individual consider cooperation right out of the gate in order to maximize credit. Mr. Waldon concluded by defining what he believes to be cooperation: (i) providing documents that the SEC cannot compel, (ii) waiving privilege in certain circumstances, (iii) translating documents to the SEC, (iv) providing financial analysis, and (v) providing a compilation of documents for the SEC. Mr. Waldon explained that cooperation does not include complying with subpoenas, providing truthful testimony, or producing documents in response to requests for production.

Ms. Bogert, contributed to the discussion of cooperation—specifically, within the Wells process. Ms. Bogert noted a productive Wells process begins before a Wells notice is issued. Ms. Bogert stressed the importance of defense counsel establishing credibility from the start and maintaining credibility throughout the process. As examples of way to lose credibility, Ms. Bogert cited unreasonable delays in responding to the SEC, witness coaching, spurious use of privilege assertions, and ignoring conflicts of interest. She noted that other enforcement colleagues have referred to such conduct "in public statements as 'lawyers behaving badly.'" Ms. Bogert concluded by stressing the importance of identifying key legal and factual issues from the start and working with the SEC staff on those key issues and not all potentially relevant issues.

Whistleblower Program

Nicole Creola Kelly, Chief of the SEC's Whistleblower Office, discussed the importance of the whistleblower program to investor protection and U.S. financial markets. Ms. Creola Kelly cited the need to have open avenues of direct communications with the SEC. She explained such direct communications should not be hindered or retaliated against by companies or investigation targets. To the extent companies do retaliate against whistleblowers, Ms. Creola Kelly explained the SEC can and will hold companies accountable. Ms. Creola Kelly then addressed confidentiality and employment agreements. Ms. Creola Kelly noted that these types of agreements cannot limit or restrict the ability of whistleblowers to speak to the SEC or require whistleblowers to forego financial incentives. She explained that such agreements must include a "carveout" for regulatory agencies, including the SEC, to permit open and direct communications, without any fear of reprisal.

Disgorgement

Olivia Choe, Chief Legal Counsel for the Division of Enforcement, discussed the remedy of disgorgement, explaining that it is a remedy in the SEC's toolkit that will be pursued aggressively. Ms. Choe explained the disgorgement remedy will be utilized to award victims compensation, as well as to divest a defendant's unjust enrichment of its wrongdoing. Ms. Choe expressed her disagreement that disgorgement is limited to pecuniary harm to the victim but rather broadly covers ill-gotten gains attributable to a defendant's actions. Ms. Choe noted that while certain judicial decisions have held that it is an abuse of discretion to award disgorgement without a finding of pecuniary harm, she emphasized that a defendant cannot avoid disgorgement altogether.

Market Sweeps

Tejal Shah, Associate Regional Director of the New York Regional Office, discussed market sweeps. Ms. Shah stated that the SEC uses sweeps as an efficient and effective way to change an industry's behavior because sweeps obtained greater attention from the targeted industry and provoked a more significant response. She cited the off-channel communications sweep as a notable example, noting that the sweep garnered significant settlement terms, including $1.7 billion in penalties and other custom settlement terms designed to rehabilitate compliance.

Ms. Shah noted several examples of other sweeps. She stated that, in 2023, the SEC conducted a sweep charging registered investment advisers for failing to comply with a new marketing rule with a compliance date of November 4, 2022. Ms. Shah remarked that it was important that the sweep was conducted less than a year after the compliance date because it is the SEC's expectation that firms will bring their policies and procedures into compliance with new rules.

Ms. Shah also noted an ongoing sweep against serial delinquent filers. She stated the latest charges were in September of 2023 and that the SEC is using data analytics to find filers who consistently fail to file on time.

Finally, Ms. Shah said that businesses should not be complacent if they are not charged in the first wave of a sweep. She also noted that, as a sweep progresses, firms could be on the hook for steeper penalties depending on the circumstances.

Auditor Actions

Glenn Gordon, Associate Regional Director of the Miami Regional Office, discussed the SEC's focus on actions against auditors. Mr. Gordon stated the SEC views auditors as amongst the most important of gatekeepers because auditors are critical to promoting public trust. He discussed a case filed last year in the Southern District of Florida against an audit firm,

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which failed to maintain independence by including in its engagement letters provisions that indemnified the firm and its personnel from liability due to knowing misrepresentations by management. Mr. Gordon stated such indemnity provisions reduced the firm's incentives to investigate representations by management during the audit process and could lead to additional disputes about whether the auditor properly did its job, if litigation later resulted from misrepresentations. He said the indemnity provisions violated Rule 2-01 of Regulation S-X, which requires that auditors be independent of their clients.

Affinity Fraud

Mr. Gordon and Jason Lee, Associate Regional Director of the San Francisco Regional Office, discussed the SEC's efforts to combat affinity fraud. Mr. Gordon stated that the efforts to combat affinity fraud have allowed his office to leverage the SEC's commitment to diversity, equity, and inclusion, including by hiring diverse staff members to help investigate fraud targeting affinity groups. He stated the cases provide an opportunity to teach investors about the signs of fraud.

Mr. Lee described the San Francisco office's efforts to combat affinity fraud, including recently charging a woman for perpetrating an $11 million scheme targeting a specific affinity group. He noted that affinity fraud cases follow a common factual pattern: a community member gaining the trust of other members, then scamming investors with promises of returns that are too good to be true.

Judicial Developments Panel

The conference also included a panel featuring several members from the Office of the General Counsel. This panel addressed recent litigation developments.

Challenges to Administrative Proceedings: *SEC v. Cochran* and *SEC v. Jarkesy*

Dominick Freda, Assistant General Counsel, discussed challenges to administrative proceedings, including *SEC v. Cochran* and *SEC v. Jarkesy*, two recent cases before the United States Supreme Court.

In *Cochran*, the Supreme Court considered whether a district court may hear a suit in which the respondent in an administrative proceeding is seeking to have the proceeding enjoined on the basis of statutory defects. The panel noted that *Cochran* questioned whether the Administrative Law Judge's ("ALJ") tenure violates Article II of the U.S. Constitution and whether the administrative adjudication process violates the due process clause. The panel described the Supreme Court's recent opinion holding district courts have jurisdiction under 28 U.S.C. § 1331 to hear cases raising structural challenges to SEC ALJ proceedings because the nature of the constitutional claim allowed for cases of this type to proceed to avoid a "here and now" injury. The panel asserted the Supreme Court limited the scope of the ruling by stating that the nature of the constitutional claim permits "extraordinary" claims like this to proceed.

Additionally, the panel discussed the Court's pending ruling in *SEC v. Jarkesy*. In that case, at the conclusion of an administrative proceeding, the ALJ held that the defendant, who controlled two hedge funds, violated the securities laws by misrepresenting numerous material aspects of his fund's supervision of those funds. The defendant appealed to the U.S. Court of Appeals for the Fifth Circuit, raising three constitutional challenges to the ALJ proceeding. The Fifth Circuit, ruling in the defendant's favor, held that Congress violated the Seventh Amendment by authorizing the SEC to award civil penalties in an Administrative Proceeding, that Congress impermissibly delegated its legislative power to the SEC by giving it the choice to seek civil penalties in an administrative proceeding or in district court, and that the statutory restriction on an ALJ's removal violates Article II of the Constitution.

The SEC sought a writ of certiorari on all three issues. The Supreme Court granted cert and held oral argument in November 2023. The panel noted that at oral argument, the Supreme Court focused primarily on the Seventh Amendment issue, but also briefly focused on the ALJ removal issue. They further stated that the Court did not focus on the non-delegation issue. The panel expects a ruling in the coming months.

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