Portfolio Media. Inc. | 111 West 19th Street, 5th Floor | New York, NY 10011 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

SEC Enforcement By The Numbers, And The End Of An Era

Law360, New York (March 10, 2017, 12:58 PM EST) --

Marc J. Fagel

Each year, hot on the heels of the federal government's Sept. 30 fiscal year-end, the U.S. Securities and Exchange Commission proclaims that it has once again filed a record (or near-record) number of enforcement actions. But the main event for true SEC nerds (yes, we exist) arrives early the following calendar year, when the agency gets around to quietly posting its more detailed enforcement report, breaking out enforcement actions by subject matter and providing other quantitative signposts.

Ordinarily, the annual statistics (or "stats" in SEC vernacular) illustrate trends that may be helpful in anticipating the future direction of the agency (and the Division of Enforcement in particular). But this, of course, is no ordinary year.

Following the November election, both SEC Chair Mary Jo White and Enforcement Division Director Andrew Ceresney departed the SEC. The five-member commission is down to a mere two commissioners — Republican appointee Michael Piwowar (serving as acting chairman) and Democratic appointee Kara Stein. The prospective chairman selected by the president (mergers and acquisitions attorney Jay Clayton) is awaiting confirmation, with the other two vacancies to be filled sometime later. Likewise, Ceresney's deputy director, Stephanie Avakian, is serving as acting enforcement director, but will presumably be replaced by someone selected by the new chairman following his confirmation.

As with other federal agencies, significant changes are on the way. While nobody expects the Enforcement Division to stop investigating violations of the federal securities laws, priorities will undoubtedly shift, as will the SEC's use of the various tools and remedies it has at its disposal. Hence, the 2016 stats are less useful as a prognosticator of things to come than a means of assessing what, if anything, has changed over the White/Ceresney era.

The Big Picture

Ceresney closed out his run at the SEC by announcing that the SEC had filed a record-breaking 868 enforcement actions in FY 2016, up nearly 8 percent from the 807 filed in 2015.[1] The agency continued the practice initiated the previous year of breaking out new "stand-alone" cases, as distinguished from more routine filings that could be viewed as padding out the results (such as "follow-on" proceedings sanctioning investment industry professionals previously sued by the SEC, or actions to deregister public companies with delinquent SEC filings). Of the 868 actions, 548 were new stand-alone cases. This number similarly outpaced the 507 new stand-alone cases from 2015.

Juxtaposed against the stats from FY 2012, the last year before Ceresney took the reins, the growth in the SEC's enforcement program is noteworthy. While stand-alone cases were not broken out at the time, the SEC filed a total of 734 cases in 2012; by 2016 that had grown nearly 20 percent. That said, the Enforcement Division also had the luxury of putting more bodies to work. In FY 2016, the division had about 1,376 employees (about a third of the SEC's staff), a 13 percent increase in boots on the ground since 2012.[2]

The growth in output from the expanded division unsurprisingly mirrors a growth in input. In 2016, the division opened 1,063 new investigations, and had 1,729 pending investigations. Four years earlier, those figures stood at 806 and 1,475, respectively — a 32 percent hike in new investigations by the end of the administration. The division also ramped up the number of formal orders of investigation (which empower the enforcement staff to subpoena documents and witness testimony), issuing 681 formal orders in 2016, up 42 percent from the 479 issued in 2012. (More on that in a moment.)

Of course, even the number of stand-alone filings is subject to interpretation. As in recent years, the division pursued some large-scale sweeps boosting the overall case count. In August, the SEC brought settled cease-and-desist proceedings against 71 municipal securities issuers as part of the agency's Municipalities Continuing Disclosure Cooperation Initiative, under which municipal bond issuers and underwriters were encouraged to come forward and self-report deficiencies in their continuing disclosures.[3] Coupled with the 14 underwriters charged in February as part of the same initiative, over 15 percent of the year's new cases consisted of these relatively straightforward proceedings.

Case Trends

The fact that the size of the overall docket has risen in recent years cannot be denied. But how have those cases been allocated across program areas?

Shortly after Ceresney and White joined the SEC in 2013, the Enforcement Division loudly heralded its reprioritization of financial reporting fraud cases. Though historically a significant part of the docket, comprising a quarter or more of all enforcement actions, financial reporting cases dropped off following the accounting fraud scandals of the early 2000s and the implementation of Sarbanes-Oxley's reforms. The dedication of significant staff resources to mortgage crisis cases beginning around 2009 further cut into the number of traditional public company cases. And while there is no question that the number of such cases has bounced back over the past few years, 2016 data show a less dramatic increase than the division may have anticipated. In FY 2012, financial reporting cases represented 13 percent of SEC enforcement actions; for FY 2015, that number had grown to 22 percent of new stand-alone actions, a marked jump. But in FY 2016, financial reporting actions slid back down to 17 percent of new cases, suggesting that the SEC may be looking harder for public-company reporting problems, but not turning up any major scandals in this area.

Another metric confirming that these cases are not seeing explosive growth is the number of officer and director bars. While these bars may be sought for many securities law violations, they are frequently seen in financial reporting cases and a useful proxy in assessing SEC attention in this area. In 2016, the SEC sought 113 officer and director bars, roughly flat with the 111 sought in 2015, and actually a decline from the 137 sought in 2012.

One caveat : In FY 2016, the SEC brought 21 new cases under the Foreign Corrupt Practices Act, or 4 percent of all new stand-alone cases, nearly double the number brought the prior year. So FCPA lawyers appear to be keeping busy.

While there has been at least some growth in financial reporting cases between 2012 and 2016, other program areas appear largely fixed. Enforcement actions against regulated entities saw a slight uptick in FY 2016, with cases against investment advisers and investment companies comprising 18 percent of the new stand-alone cases (versus 15 percent in 2015) and cases against broker-dealers coming in at 11 percent (versus 8 percent). Notably, when both stand-alone and follow-on actions are considered, cases against regulated entities and individuals constitute nearly half of all enforcement filings, which is essentially unchanged from 2012.

Closing out the other main components of the enforcement program, we find that insider trading cases clocked in at 8 percent of new stand-alone cases in 2016 (largely unchanged from 2015, but a bit lower than the 10 percent seen in 2012); offering frauds represented about 16 percent of new cases in 2016 (versus 18 percent in 2015 and 15 percent in 2012); and market manipulation cases represented about 5.5 percent of new cases (down from about 8 percent in 2015 and 2012).

Overall, one could conclude that, aside from a small increase in financial reporting cases, the Ceresney/White years did not introduce significant changes in the types of cases pursued by the Enforcement Division. There were minor fluctuations, but for the most part, the breakdown across program areas was somewhat predictable. Indeed, the only significant anomaly in the data is the huge increase in the number of cases involving municipal securities. However, as noted earlier, the numbers here reflect the continuing disclosure initiative, which netted about 150 cases against issuers and underwriters in 2015 and 2016; aside from those sweeps, cases involving municipal securities, while growing, remain a small component of the program.

Looking Forward

With the SEC in a state of flux, it can be dangerous to wade too deeply into prognostication. New leadership can be unpredictable, and unexpected crises have a way of derailing the best-laid plans. Just over 15 years ago, an incoming SEC chair famously promised to make the SEC a "kinder and gentler place" for accountants; not long thereafter, Enron collapsed and SEC priorities were turned on their head.

Still, some significant changes appear likely. First, the frenetic pace of new enforcement actions under Ceresney and White will undoubtedly slow down. The growth of the enforcement staff that drove some of those numbers is sure to level off, if not decline, under the budget numbers being proposed by the new administration. Moreover, Acting Chairman Piwowar has already taken steps to rein in the enforcement program, reportedly curtailing the authority of senior leaders in the division to instantaneously issue formal orders of investigation (a post-Madoff reform intended to allow the division to move more swiftly without awaiting authorization from the full commission).[4] Likewise, Piwowar has in the past questioned White's "broken windows" approach of chasing down technical, nonfraud violations more traditionally left to comment letters from the Division of Corporation Finance or other means of correction short of full-blown enforcement actions.[5] These violations contributed to a number of the high-volume sweeps that dramatically inflated enforcement stats in recent years, and one can imagine these being curbed under the new administration.

Other changes from the past few years may also be revisited. The SEC's increasing use of its administrative forum rather than federal court for litigated actions, which was a significant (and controversial) strategic change during the Ceresney years, has already slowed somewhat in the wake of public criticism and some adverse court rulings. The Tenth Circuit recently held that the SEC's manner of appointing its administrative law judges runs afoul of the appointments clause of the U.S. Constitution; the D.C. Circuit, which had upheld the practice earlier in the year, subsequently granted en banc review.[6] Given both legal uncertainty and ongoing fairness concerns, it would not be unexpected for the SEC to return to using administrative proceedings primarily for actions involving regulated entities, and turning largely to federal court for financial fraud, insider trading and other matters.

Exacting significant financial penalties on public companies will also receive more scrutiny under a new administration. While the Enforcement Division has pushed for ever-increasing penalties in recent years — the 2016 stats report proclaimed over $1.25 billion in penalties ordered that year — critics of the current approach, including Piwowar, are much more sensitive to concerns about penalizing shareholders for the misconduct of executives.

Finally, whether the requirement that selected parties admit misconduct as a condition of settlement — an innovation implemented by Ceresney and White — survives into the new administration is an open question. Such admissions remain a relative rarity, and as a result have proven less controversial than other aggressive stances taken in recent years.

—By Marc J. Fagel, Gibson, Dunn & Crutcher LLP

Marc Fagel is a partner in Gibson Dunn's San Francisco office and co-chair of the firm's securities enforcement practice group. Prior to joining the firm, Fagel spent more than 15 years with the SEC's San Francisco Regional Office, most recently serving as regional director from 2008 to 2013.

Christina Yang, an associate in Gibson Dunn's Palo Alto, California, office, assisted in the preparation of this article.

DISCLOSURE: Fagel is a counsel of record in Lucia v. SEC, the D.C. Circuit case mentioned here.

[1] SEC Press Release, SEC Announces Enforcement Results for FY 2016 (Oct. 11, 2016), available at www.sec.gov/news/pressrelease/2016-212.html; Select SEC and Market Data, Fiscal 2016 (Jan. 18, 2017), available at www.sec.gov/reportspubs/select-sec-and-market-data/secstats2016.pdf. Unless otherwise noted, the data used herein are drawn from the annual Select SEC and Market Data posted on the SEC's website.

[2] Compare SEC's FY 2017 Congressional Justification (Feb. 9, 2016), available at www.sec.gov/about/reports/secfy17congbudgjust.pdf; FY 2014 Congressional Budget Justification (Apr. 10, 2013), available at www.sec.gov/about/reports/secfy14congbudgjust.shtml.

[3] SEC Press Release, SEC Charges 71 Municipal Issuers in Muni Bond Disclosure Initiative (Aug. 24, 2016), available at www.sec.gov/news/pressrelease/2016-166.html.

[4] Sarah Lynch, SEC's Acting Chair Scales Back Enforcement unit's Subpoena Powers, Reuters (Feb. 16, 2017).

[5] Commissioner Piwowar, Remarks to the Securities Enforcement Forum 2014 (Oct. 14, 2014),

available at www.sec.gov/News/Speech/Detail/Speech/1370543156675 (“If every rule is a priority, then no rule is a priority”).

[6] Bandimere v. SEC, No. 15-9586 (10th Cir. Dec. 27, 2016); Lucia v. SEC, 832 F. 3d 277 (D.C. Cir. 2016), reh’g en banc petition granted (Feb. 16, 2017).
