

October 31, 2017

## **Recent Public Remarks by Co-Directors of SEC Enforcement Division Signal Potential Changing Enforcement Priorities**

Recent public remarks by Steven Peikin and Stephanie Avakian, Co-Directors of the Division of Enforcement of the U.S. Securities and Exchange Commission, suggest a potential shifting of enforcement priorities and emphasis.

In remarks during an October 26, 2017 panel at the Securities Enforcement Forum in Washington, D.C., Co-Director Peikin commented on the “broken windows” approach to securities enforcement advocated by former Commission Chair Mary Jo White.

In a 2013 speech at the Securities Enforcement Forum, then-Chair White described the “broken windows” approach as follows:

The theory is that when a window is broken and someone fixes it—it is a sign that disorder will not be tolerated. But, when a broken window is not fixed, it “is a signal that no one cares, and so breaking more windows costs nothing.” The same theory can be applied to our securities markets—minor violations that are overlooked or ignored can feed bigger ones, and, perhaps more importantly, can foster a culture where laws are increasingly treated as toothless guidelines. And so, I believe it is important to pursue even the smallest infractions.<sup>1</sup>

Last week’s comments by Peikin suggest a potential shift away from a focus on “minor” or technical violations of the securities laws by the Enforcement Division. In particular, Peikin stated that the Division of Enforcement is likely to take a “more selective approach,” focusing on bringing “a few cases” on a particular issue to send a broader message and de-emphasizing extensive industry-wide sweeps or enforcement actions based on technical violations of the federal securities laws. These comments by Peikin appear to be consistent with prior statements of the new Chairman of the Commission, Jay Clayton. During his confirmation hearings, for example, Chairman Clayton expressed concern about the Division of Enforcement’s approach to corporate penalties, noting that “[s]hareholders do bear those costs and we have to keep that in mind.”<sup>2</sup>

---

<sup>1</sup> Mary Jo White, *Remarks at the Securities Enforcement Forum* (Oct. 9, 2013), available at <https://www.sec.gov/news/speech/spch100913mjw>.

<sup>2</sup> Dave Michaels & Andrew Ackerman, SEC Chairman Nominee Jay Clayton Calls for Scaling Back Regulations to Encourage IPOs, *Wall St. J.*, Mar. 23, 2017.

Peikin further suggested the Division of Enforcement may de-emphasize settlements requiring admissions of wrongdoing. Peikin expressed doubts about the wisdom of insisting on admissions where other elements of appropriate relief are available as part of a settlement. As a practical matter, the effect of any changes in this approach may be limited. According to one academic study, forthcoming in the *Iowa Law Review*, only 2% of cases filed between 2014 and 2017 resulted in such admissions. Although Peikin noted that the Division may still seek admissions of wrongdoing in certain circumstances, including when a defendant has pleaded guilty to criminal offenses related to the same underlying conduct, the traditional “neither admit, nor deny” settlement is likely to remain the rule in settled enforcement proceedings.

During his remarks, Peikin also noted a potential reduction in resources that could affect enforcement activity. Peikin indicated that current budget constraints will not allow the Division to replace investigators and attorneys who are likely to leave as the result of normal attrition.

In a separate keynote speech at the Securities Enforcement Forum, Co-Director Avakian described a “year of transition” for the Division and described two new specialized units: a retail unit and a cyber unit, both of which are intended to “align . . . [the Division’s] resources with two . . . key priorities.”<sup>3</sup>

The Retail Strategy Task Force, according to Avakian, will focus on “the intersection of investment professionals and retail investors.” Avakian cited a number of recent enforcement actions aimed at the types of conduct that the Retail Strategy Task Force will target, including proceedings involving fees, disclosures, and the suitability of investment products sold to retail investors. In describing the goals of the Retail Strategy Task Force, Avakian emphasized that “[t]he premise that there is trade-off between ‘Wall Street’ and ‘Main Street’ enforcement is a false one,” citing other recent enforcement actions targeting issuers and large financial institutions.

Avakian also described the Enforcement Division’s new Cyber Unit, the first new specialized unit since the creation of the five original specialized units—Asset Management, Market Abuse, Structured and New Products, Foreign Corrupt Practices Act, and Municipal Securities and Public Pensions—as part of the 2010 reorganization of the Division of Enforcement. The newly-created Cyber Unit will focus on three areas: (1) cyber-related conduct involving efforts to obtain market advantages, (2) failures by registered entities to appropriately safeguard against cybersecurity threats, and (3) cyber-related disclosure failures by public companies.

In her speech, Avakian noted that the Division has not previously brought an action based on a public company’s failure to disclose cybersecurity-related risks, but cautioned that the Division of Corporation

---

<sup>3</sup> Stephanie Avakian, *The SEC Enforcement Division’s Initiatives Regarding Retail Investor Protection and Cybersecurity* (Oct. 26, 2017), available at <https://www.sec.gov/news/speech/speech-avakian-2017-10-26>.

Finance has “frequently reminded registrants” of their disclosure obligations with respect to cybersecurity risks and observed that such disclosures “are often material on their own or necessary in order to make other disclosures, in light of the circumstances under which they are made, not misleading.”

Finally, although not a designated area of focus, block chain technology is another area Avakian said warranted a “consistent, thoughtful approach” that would be facilitated by the creation of the Cyber Unit.

The recent comments by the Co-Directors of the Division of Enforcement suggest that there may be significant changes in the enforcement environment under the new leadership at the Commission. In particular, it can be expected that the “broken windows” strategy of allocating significant enforcement resources to minor violations will no longer be a favored approach. The combination of skepticism toward corporate penalties and a reduced emphasis on admissions in the context of settled proceedings also could potentially lead toward a changed dynamic in negotiating enforcement resolutions. Finally, budget constraints could lead to a reduction in enforcement resources. It should be noted, however, that the enforcement of scienter-based fraud continues to be a prominent and high priority area for the Division of Enforcement, with an increased emphasis on the protection of retail investors and cybersecurity issues, alongside more traditional scienter-based matters.

\* \* \*

This memorandum is not intended to provide legal advice, and no legal or business decision should be based on its content. Questions concerning issues addressed in this memorandum should be directed to:

Jessica S. Carey  
+1-212-373-3566  
[jcarey@paulweiss.com](mailto:jcarey@paulweiss.com)

Andrew J. Ehrlich  
+1-212-373-3166  
[aehrich@paulweiss.com](mailto:aehrich@paulweiss.com)

Michael E. Gertzman  
+1-212-373-3281  
[mgertzman@paulweiss.com](mailto:mgertzman@paulweiss.com)

Michele Hirshman  
+1-212-373-3747  
[mhirshman@paulweiss.com](mailto:mhirshman@paulweiss.com)

Brad S. Karp  
+1-212-373-3316  
[bkarp@paulweiss.com](mailto:bkarp@paulweiss.com)

Daniel J. Kramer  
+1-212-373-3020  
[dkramer@paulweiss.com](mailto:dkramer@paulweiss.com)

Lorin L. Reisner  
+1-212-373-3250  
[lreisner@paulweiss.com](mailto:lreisner@paulweiss.com)

Walter G. Ricciardi  
+1-212-373-3350  
[wricciardi@paulweiss.com](mailto:wricciardi@paulweiss.com)

Audra J. Soloway  
+1-212-373-3289  
[asoloway@paulweiss.com](mailto:asoloway@paulweiss.com)

Richard C. Tarlowe  
+1-212-373-3035  
[rtarlowe@paulweiss.com](mailto:rtarlowe@paulweiss.com)

*Associates James H. Borod and Stephen Thompson contributed to this Client Memorandum.*