

January 25, 2022

SEC Enforcement: Year in Review

2021 was a year of transition and recalibrated priorities for the Enforcement Division. Under the leadership of Chair Gary Gensler and Director of Enforcement Gurbir Grewal, several key areas came into focus that will impact businesses across sectors. In this year-end review, we highlight important takeaways for business leaders and in-house counsel from the Division's activities in 2021, and what these activities mean for the Division's priorities for the year ahead.

Highlights:

- **Changes to Enforcement Practices and Policies:** Chair Gensler and Director of Enforcement Grewal announced potentially significant changes to SEC enforcement practices and policies, including by requiring parties to make admissions of wrongdoing in cases involving "egregious" misconduct and by potentially limiting the involvement of Division leadership in the Wells process in certain cases.
- **Untested Positions Regarding Cryptocurrency:** The SEC is taking an untested view that various forms of digital assets are securities subject to, among other things, the registration requirements of the securities laws. This has led to actions pursuing digital assets with novel enforcement theories and a correspondingly predictable uptick in litigated cases, including litigation centered around whether particular cryptocurrencies are in fact securities.
- **Focus on SPAC Transactions:** The Division highlighted in public statements that it will closely scrutinize, among other things, disclosures around conflicts of interest and the differing economic interests of SPAC sponsors, directors, officers and their affiliates as compared to the interests of the SPAC's public shareholders. Enforcement activity in this area in 2021 also scrutinized SPAC internal controls and the sufficiency of diligence on merger targets.
- **Increase in Climate and ESG Disclosures:** Chair Gensler spoke frequently about ESG as a priority, including the need to enhance disclosures of climate risk for public companies and of investment funds that market themselves as "sustainable." The Division did not file any enforcement actions in this area in 2021 but public reports indicate that there are several active investigations underway.
- **Trends in Insider Trading, Cybersecurity and Digital Recordkeeping:** There were a number of other trends in enforcement activity in 2021, including the use of novel legal theories in several insider trading cases, significant attention to disclosure and internal control requirements related to cybersecurity violations, and a focus on recordkeeping issues at financial institutions and broker dealers related to the use of personal devices and messaging platforms.

SEC Chair Gensler and SEC Director of Enforcement Grewal

Chair Gary Gensler, the former Obama Administration CFTC chair, was confirmed in April 2021. Director of Enforcement Gurbir Grewal, who had been serving as the Attorney General of New Jersey and prior to that had been a federal and local prosecutor, was appointed in July 2021. Indications are that Chair Gensler and Director Grewal intend to pursue an aggressive enforcement strategy, including through policies of seeking admissions of wrongdoing in certain settlements and reworking and potential limiting of the Wells process.¹

Requiring Admissions

In his October 13, 2021 speech announcing these new policies, Director Grewal stated that “[w]hen it comes to accountability, few things rival the magnitude of wrongdoers admitting that they broke the law, and so, in an era of diminished trust, we will, in appropriate circumstances, be requiring admissions in cases where heightened accountability and acceptance of responsibility are in the public interest.”² SEC Enforcement Division deputy director Sanjay Wadhwa has explained that the Division plans to seek such admissions “in cases involving egregious misconduct and where a large number of investors were harmed or where defendants obstructed the SEC’s investigation.”³

It remains unclear how much of an impact this stated change will have on settlements. The SEC announced a similar policy shift in 2013 under former chair Mary Jo White,⁴ but settlements requiring admissions of wrongdoing remained the exception; between 2014 and 2016, only 2% of SEC settlements involved admissions of wrongdoing.⁵ To date, there have not been any publicly filed enforcement actions under the new regime that have included an admission of wrongdoing.

Curtailing the Wells Process

Director Grewal also has indicated that senior leadership of the Enforcement Division may not participate personally in meetings with counsel during the Wells process to the same extent as has been traditionally expected, particularly in cases that do not “present novel legal or factual questions, or raise significant programmatic issues.”⁶ Instead, the Director and Deputy Director generally plan to deputize Wells meetings to direct reports and SEC staff.⁷ The stated goal of this policy is to make the Wells process “more streamlined and efficient,”⁸ by not having the Director or Deputy Director regularly participate in these meetings. However, decentralizing the process reduces programmatic consistency, increases the risk that similar matters may reach

¹ See Gurbir Grewal, Director, Division of Enforcement, Remarks at SEC Speaks 2021 (Oct. 13, 2021), <https://www.sec.gov/news/speech/grewal-sec-speaks-101321>; Paul Weiss Publication, SEC Enforcement Director Announces ‘Aggressive’ Policy Shifts, Including Requiring Admissions of Wrongdoing (Oct. 18, 2021), <https://www.paulweiss.com/practices/litigation/white-collar-regulatory-defense/publications/sec-enforcement-director-announces-aggressive-policy-shifts-including-requiring-admissions-of-wrongdoing?id=41395>.

² Gurbir Grewal, Director, Division of Enforcement, Remarks at SEC Speaks 2021 (Oct. 13, 2021), <https://www.sec.gov/news/speech/grewal-sec-speaks-101321>.

³ Dave Michaels, *Wall Street, Companies May Have to Give Up More to Settle With SEC*, WALL ST. J. (Oct. 12, 2021), <https://www.wsj.com/articles/sec-to-see-admissions-of-wrongdoing-in-some-enforcement-actions-11634139229>.

⁴ Mary Jo White, SEC Chair, *Deploying the Full Enforcement Arsenal*, Council of Institutional Investors Fall Conference in Chicago, IL (Sept. 26, 2013), <https://www.sec.gov/news/speech/spch092613mjw>.

⁵ David Rosenfeld, Admissions in SEC Enforcement Cases: The Revolution That Wasn’t, 103 Iowa L. Rev. 113 (2017), <https://ilr.law.uiowa.edu/print/volume-103-issue-1/admissions-in-sec-enforcement-cases-the-revolution-that-wasnt/>.

⁶ Gurbir Grewal, Director, Division of Enforcement, Remarks at SEC Speaks 2021 (Oct. 13, 2021), <https://www.sec.gov/news/speech/grewal-sec-speaks-101321>.

⁷ *Id.*

⁸ *Id.*

inconsistent results, and reduces opportunities for discussion about the practical significance and consequences of enforcement actions.⁹

SEC Chair Gensler's Areas of Focus

Chair Gensler has repeatedly emphasized his plan to focus increased resources and attention on issues related to cryptocurrency, special purpose acquisition companies ("SPACs"), and climate and Environmental, Social, & Governance ("ESG") issues.

Cryptocurrency

As the cryptocurrency market has grown significantly, Chair Gensler has compared it to "the Wild West or the old world of 'buyer beware' that existed before the securities laws were enacted,"¹⁰ and urged crypto exchanges to register with the SEC. He has warned that "financial innovations throughout history don't long thrive outside of public policy frameworks."¹¹ Chair Gensler has also expressed concerns that crypto can be used to subvert anti-money laundering, sanctions, and tax collection laws.¹² Chair Gensler has stated that the SEC intends to fill these regulatory gaps by identifying how existing legal authority can be applied to this market and where new laws are needed.¹³

Even as new regulations are needed in his view, Chair Gensler has warned that market participants that use crypto to engage in securities transactions, as well as asset managers that invest in crypto assets, must comply with federal securities laws.¹⁴ Chair Gensler has encouraged parties currently engaged in operating crypto platforms or issuing crypto tokens to be proactive in working with the SEC to discuss any challenges with coming into compliance with federal securities laws.¹⁵

2021 Enforcement

Several novel cryptocurrency enforcement actions brought by the SEC in 2021 highlighted the threshold question of which digital assets and platforms qualify as securities under the test set forth in the seminal 1946 Supreme Court case *SEC v. W.J. Howey Co.* *Howey* provides that a transaction is an investment contract and therefore subject to the securities laws when it is (1) an investment of money; (2) in a common enterprise; (3) with the expectation of profit; (4) to be derived from the efforts of others.¹⁶

In a few high profile enforcement actions, the SEC did not provide a clear articulation as to why the digital assets at issue qualified as securities, resulting in criticism of the Commission from a number of corners including from some of the Commissioners themselves. For example, in *In the Matter of Biotics LTD. f/d/b/a Coinschedule LTD.*, the SEC settled charges against a company that ran a website that publicized digital token offerings but did not disclose that the issuers of these tokens

⁹ For further discussion of these issues, see Paul Weiss Publication, SEC Enforcement Director Announces 'Aggressive' Policy Shifts, Including Requiring Admissions of Wrongdoing (Oct. 18, 2021), <https://www.paulweiss.com/practices/litigation/white-collar-regulatory-defense/publications/sec-enforcement-director-announces-aggressive-policy-shifts-including-requiring-admissions-of-wrongdoing?id=41395>.

¹⁰ Gary Gensler, SEC Chair, Testimony Before the United States Senate Committee on Banking, Housing, and Urban Affairs (Sept. 14, 2021), <https://www.sec.gov/news/testimony/gensler-2021-09-14>.

¹¹ Gary Gensler, SEC Chair, Remarks Before the European Parliament Committee on Economic and Monetary Affairs (Sept. 1, 2021), <https://www.sec.gov/news/speech/gensler-remarks-european-parliament-090121>.

¹² Gary Gensler, SEC Chair, Remarks Before the Aspen Security Forum (Aug. 3, 2021), <https://www.sec.gov/news/public-statement/gensler-aspen-security-forum-2021-08-03>.

¹³ Gary Gensler, SEC Chair, Testimony Before the Subcommittee on Financial Services and General Government, U.S. House Appropriations Committee (May 26, 2021), <https://www.sec.gov/news/testimony/gensler-2021-05-26>.

¹⁴ *Id.*; see also Gary Gensler, SEC Chair, Remarks Before the European Parliament Committee on Economic and Monetary Affairs (Sept. 1, 2021), <https://www.sec.gov/news/speech/gensler-remarks-european-parliament-090121>.

¹⁵ Gary Gensler, SEC Chair, Remarks Before the Investor Advisory Committee (Dec. 2, 2021), <https://www.sec.gov/news/statement/gensler-iac-statement-120221>.

¹⁶ *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946).

paid the website to be profiled and publicized.¹⁷ Commissioners Hester M. Peirce and Elad Roisman issued a public statement criticizing the SEC’s failure to provide clear guidance as to when a digital currency is in fact a security, labeling the Commission’s approach as “clue-by-enforcement.”¹⁸ Commissioners Peirce and Roisman wrote that they were “disappointed that the Commission’s settlement with Coinschedule did not explain *which* digital assets touted by Coinschedule were securities, an omission which is symptomatic of our reluctance to provide additional guidance about how to determine whether a token is being sold as part of a securities offering or which tokens are securities.”¹⁹

Similarly, in *In the Matter of Poloniex LLC*, the SEC alleged that an unregistered trading platform through which parties could buy and sell digital assets met the definition of an “exchange” because it “provided the non-discretionary means for trade orders to interact and execute through the combined use of the Poloniex website, an order book, and the Poloniex trading engine.”²⁰ Notably, the SEC did not identify what digital asset that traded on the platform in fact qualified as a security, instead stating in conclusory fashion that Poloniex facilitated trading of “digital assets that were investment contracts and therefore securities.”²¹

On the other hand, in *In the Matter of Blockchain Credit Partners d/b/a DeFi Money Market et al.*, the first SEC enforcement involving decentralized financial (“DeFi”) technology, the SEC articulated an aggressive view as to why the digital assets at issue satisfied the *Howey* test.²² DeFi Money Market (“DMM”) sold two types of digital tokens: mTokens (which paid interest to investors) and DMG “governance tokens” (which, among other things, gave holders certain voting rights and could be resold on the secondary market).²³ The SEC alleged that the mTokens were investment contracts under the *Howey* test in part because purchasers had a reasonable expectation of future profit in the form of interest upon redemption.²⁴ The SEC further alleged that the DMG tokens were securities under *Howey* because there was a reasonable expectation of profits through, among other things, a trading market for the tokens.²⁵ Interestingly, the SEC Order alleged that the DMG tokens satisfied the “effort of others” element of *Howey* even though holders of DMG tokens had voting rights as to several aspects of DMM’s business.²⁶

Of potential significance to enforcement activity in this space in 2022 and beyond, in November 2021 a jury for the first time assessed whether a particular digital asset was a security under *Howey* and concluded that it was not. In *Audet v. Fraser*, a civil litigation in the District of Connecticut to which the SEC was not a party, the jury found that a physical crypto mining hardware sold to customers who would use its computing power to “mine” for virtual currency, was *not* a security.²⁷ Of particular significance, the court instructed the jury on the fourth element of the *Howey* test—often the most hotly contested element—that “[i]f there was a reasonable expectation of significant investor control, then profits would not be considered derived solely from the efforts of others,” but “if the expectation was that the participants would be passive investors, then profits would be

¹⁷ *In the Matter of Biotics LTD. f/d/b/a Coinschedule LTD.*, Order Instituting Cease-and-Desist Proceedings Pursuant to Section 8A of the Securities Act of 1933, Making Findings, and Imposing a Cease-and-Desist Order, Sec. Act. Rel. No. 10956, Admin. Proc. File No. 3-20398 (July 14, 2021), <https://www.sec.gov/litigation/admin/2021/33-10956.pdf>.

¹⁸ Hester M. Peirce and Elad L. Roisman, SEC Commissioners, In the Matter of Coinschedule (July 14, 2021), <https://www.sec.gov/news/public-statement/peirce-roisman-coinschedule>.

¹⁹ *Id.*

²⁰ SEC Press Release, SEC Charges Poloniex for Operating Unregistered Digital Asset Exchange (Aug. 9, 2021), <https://www.sec.gov/news/press-release/2021-147>; *In the Matter of Poloniex, LLC*, Order Instituting Cease-and-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order, Exchange Act Rel. No. 92607, Admin. Proc. File No. 3-20455 (Aug. 9, 2021), <https://www.sec.gov/litigation/admin/2021/34-92607.pdf>.

²¹ SEC Press Release, SEC Charges Poloniex for Operating Unregistered Digital Asset Exchange (Aug. 9, 2021), <https://www.sec.gov/news/press-release/2021-147>.

²² *In the Matter of Blockchain Credit Partners d/b/a DeFi Money Market et al.*, Order Instituting Cease-and-Desist Proceedings, Pursuant to Section 8A of the Securities Act of 1933 and Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order, Sec. Act. Rel. No. 10961, Exchange Act Rel. No. 92588, Admin. Proc. File No. 3-20453 (Aug. 6, 2021), <https://www.sec.gov/litigation/admin/2021/33-10961.pdf>.

²³ *Id.* at 2.

²⁴ *Id.* at 10-11.

²⁵ *Id.* at 9-10.

²⁶ *Id.* at 2, 10-11.

²⁷ *Audet v. Fraser*, No. 3:16-cv-940, ECF No. 330 at 2 (D. Conn. Nov. 2, 2021).

considered derived solely from the efforts of others.”²⁸ This interpretation of the fourth element could undermine the SEC’s ability to characterize certain digital assets as securities because investors in cryptocurrency often have a reasonable expectation of significant control.

In 2022, we expect to see continued aggressive enforcement activity around threshold questions of which digital assets qualify as securities under *Howey* and which platforms qualify as exchanges. This will likely lead to a continued uptick in litigation with the SEC in 2022.

SPACs

The number of SPAC transactions, which Chair Gensler refers to as “SPAC blank-check IPO[s],” has “ballooned by nearly 10 times between 2019 and 2021” and “SPAC blank-check IPOs now account for more than three-fifths of all U.S. IPOs.”²⁹ In 2021, there were 181 de-SPAC transactions, which Chair Gensler terms the “SPAC target IPO,” with a total deal value of \$370 billion, up from only 26 SPAC target IPOs in 2019.³⁰ Chair Gensler has flagged several areas of de-SPAC transactions that he wants to be the focus of enhanced rulemaking and/or enforcement activity.

Disclosure guidance, including of fees, sponsor compensation, dilution, and potential conflicts of interest

Chair Gensler has warned that retail investors must be given “the appropriate and accurate information they need”³¹ at both stages of SPAC transactions, and has called for rulemakings requiring “enhanced disclosures” and “economic analysis to better understand how investors are advantaged or disadvantaged by SPAC transactions.”³² Chair Gensler has expressed concerns that “[d]ue to the various moving parts and SPACs’ two-step structure,” “these vehicles may have additional conflicts inherent to their structure,” including “between the investors who vote then cash out” after the first stage “and those who stay through the deal.”³³ He has also raised questions about the “costs” that the SPAC “structure is bearing — whether sponsor fees, dilution from the [second stage] investors, and fees for investment banks or financial advisers” and whether these costs “are coming out of the retail public’s investment dollars.”³⁴ He has asked “staff for recommendations about how we might update our rules so that investors are better informed about the fees, costs, and conflicts that may exist with SPACs.”³⁵

In line with these concerns, the Division of Corporation Finance issued disclosure guidance clarifying the disclosures required around conflicts of interest and the differing economic interests of SPAC sponsors, directors, officers and their affiliates as compared to the interests of the SPAC’s public shareholders.³⁶ Based on this guidance, SPACs should consider the following issues in IPO registration statements: potential conflicts of interest, especially on the part of the SPAC insiders; the limited time that a SPAC has to complete a business transaction and its impact; the compensation and role of the underwriters; the economic terms of SPAC insider investments; and the terms of SPAC issuances to its sponsor and others in private financings.³⁷ SPACs should also make clear disclosures on the following issues in their business combination filings with the SEC: additional financing

²⁸ *Audet v. Fraser*, No. 3:16-cv-940, ECF No. 326 at 21-22 (D. Conn. Oct. 29, 2021).

²⁹ Gary Gensler, SEC Chair, Remarks Before the Healthy Markets Association Conference (Dec. 9, 2021), <https://www.sec.gov/news/speech/gensler-healthy-markets-association-conference-120921>.

³⁰ *Id.*

³¹ Gary Gensler, SEC Chair, Testimony Before the Subcommittee on Financial Services and General Government, U.S. House Appropriations Committee (May 26, 2021), <https://www.sec.gov/news/testimony/gensler-2021-05-26>.

³² Gary Gensler, SEC Chair, Prepared Remarks Before the Investor Advisory Committee (Sept. 9, 2021), <https://www.sec.gov/news/public-statement/gensler-iac-2021-09-09>.

³³ Gary Gensler, SEC Chair, Remarks Before the Healthy Markets Association Conference (Dec. 9, 2021), <https://www.sec.gov/news/speech/gensler-healthy-markets-association-conference-120921>.

³⁴ Gary Gensler, SEC Chair, Prepared Remarks Before the Small Business Capital Formation Advisory Committee (Sept. 27, 2021), <https://www.sec.gov/news/public-statement/gensler-sbcfac-2021-09-27>.

³⁵ *Id.*

³⁶ SEC Disclosure Guidance, *Special Purpose Acquisition Companies* (Dec. 22, 2020), <https://www.sec.gov/corpfin/disclosure-special-purpose-acquisition-companies>.

³⁷ *Id.*

and dilution; interests of SPAC insiders in evaluating the transaction and other opportunities; and underwriters' services and fees.³⁸

Although there were not any enforcement actions brought concerning SPACs in these areas in 2021, we expect this to be an area of focus for the Enforcement Division in 2022.

Marketing practices, including celebrity endorsements

Chair Gensler has also raised concerns that "SPAC target IPOs often are announced with a slide deck, a press release, and even celebrity endorsements" such that "[t]he value of SPAC shares can move dramatically based on incomplete information, long before a full disclosure document or proxy is filed" and "[i]nvestors may be making decisions based on incomplete information or just plain old hype."³⁹ Chair Gensler has asked his staff to make recommendations "around how to guard against what effectively may be improper conditioning of the SPAC target IPO market," including by requiring "more complete information at the time that a SPAC target IPO is announced."⁴⁰

Auditor considerations and other gatekeeper obligations

Chair Gensler has also focused on whether auditors and other gatekeepers are serving their role as rigorously in SPAC transactions as they do in traditional IPOs. He has warned that "[m]any gatekeepers carry out functionally the same role as they would in a traditional IPO but may not be performing the due diligence [in SPACs] that we've come to expect."⁴¹ He has sought staff recommendations about how the SEC "can better align incentives between gatekeepers and investors, and how [it] can address the status of gatekeepers' liability obligations."⁴²

Financial reporting, internal control, and corporate governance

SEC leadership has also warned that financial reporting, internal control, and corporate governance requirements should apply to companies that go public through a SPAC just as they do to companies who go public through traditional IPOs. The SEC has warned that public company requirements, including books and records and internal control requirements, apply to SPACs before and after the business combination.⁴³ The SEC has further cautioned that "[c]orporate board oversight is essential prior to, during, after the de-SPAC merger," including the independence, experience, and clear roles of board members and particularly of the Audit Committee.⁴⁴

³⁸ *Id.*

³⁹ Gary Gensler, SEC Chair, Remarks Before the Healthy Markets Association Conference (Dec. 9, 2021), <https://www.sec.gov/news/speech/gensler-healthy-markets-association-conference-120921>.

⁴⁰ *Id.*

⁴¹ *Id.*

⁴² *Id.*

⁴³ SEC Division of Corporation Finance, Staff Statement on Select Issues Pertaining to Special Purpose Acquisition Companies (Mar. 31, 2021), <https://www.sec.gov/news/public-statement/division-cf-spac-2021-03-31>.

⁴⁴ Paul Munter, Acting Chief Accountant, Financial Reporting and Auditing Considerations of Companies Merging with SPACs (Mar. 31, 2021), <https://www.sec.gov/news/public-statement/munter-spac-20200331>; see also SEC Division of Corporation Finance, Staff Statement on Select Issues Pertaining to Special Purpose Acquisition Companies (Mar. 31, 2021), <https://www.sec.gov/news/public-statement/division-cf-spac-2021-03-31> ("The combined company also must meet qualitative standards regarding corporate governance, such as requirements regarding a majority independent board of directors, an independent audit committee consisting of directors with specialized experience, independent director oversight of executive compensation and the director nomination process, and a code of conduct applicable to all directors, officers, and employees.").

SPAC-Related Enforcement Activity in 2021

Publicly filed enforcement actions in the SPAC space in 2021 focused principally on matters involving allegedly materially misleading statements about the proposed transaction and have, among other things, highlighted the SEC's focus on the sufficiency of the due diligence by the SPAC into its merger target.

In July 2021, the SEC brought the first enforcement proceeding of the recent SPAC boom in *In the matter of Momentus, Inc.*, against a SPAC, its sponsor, its merger target and certain executives.⁴⁵ The charges stemmed from allegedly false and misleading claims made by the merger target about its business to the SPAC, Stable Road, which Stable Road then repeated to investors. The SEC Order focused on, among other things, Stable Road's and its sponsors' allegedly inadequate due diligence to confirm the veracity of the merger target's statements before repeating those statements to investors.⁴⁶

The SEC has since brought additional SPAC-related enforcement actions including against Akazoo S.A., a music streaming business, for allegedly defrauding investors by making false claims about its user base, operations, and revenue,⁴⁷ and against others for allegedly defrauding investors through information provided through social media communications and media appearances by executives regarding product and technological milestones.

Looking ahead, we expect to see a continued focus by the Enforcement Division on SPACs and de-SPAC transactions including matters involving allegedly inadequate disclosures, including inadequate disclosure of conflicts and fees, and enforcement actions centered around allegedly inadequate due diligence and internal controls.

Climate/ESG

Chair Gensler has repeatedly made clear that ESG issues, in particular sustainability and climate change related issues, will be a key focus of regulation and enforcement activity under his leadership. In March 2021, the Commission announced the creation of a Climate and ESG Task Force within the Division of Enforcement, a 22-member body led by then-Acting Deputy Director of Enforcement, Kelly L. Gibson. The task force's initial focus is to "identify any material gaps or misstatements in issuers' disclosure of climate risks under existing rules," as well as to "analyze disclosure and compliance issues relating to investment advisers' and funds' ESG strategies."⁴⁸

Chair Gensler has directed SEC staff to work on two key proposed rule changes related to climate risk disclosures, one focused on public companies and the other on investment funds.⁴⁹

- **Public Companies:**

Similar to previous additions to disclosure requirements related to management discussion and analysis and executive compensation, the SEC seeks to add similar disclosure requirements surrounding climate risk.⁵⁰ Chair Gensler has directed SEC

⁴⁵ *In the matter of Momentus, Inc.*, Order Instituting Cease-and-Desist Proceedings, Pursuant to Section 8A of the Securities Act of 1933 and Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order, Sec. Act. Rel. No. 10955, Exchange Act Rel. No. 92391, Admin. Proc. File No. 3-20393 (July 13, 2021), <https://www.sec.gov/litigation/admin/2021/33-10955.pdf>.

⁴⁶ *Id.* at 2-3.

⁴⁷ SEC Press Release, Post-SPAC Music Streaming Company Reaches \$38.8 Million Settlement in Ongoing Fraud Action (Oct. 27, 2021), <https://www.sec.gov/news/press-release/2021-216>.

⁴⁸ See Press Release, SEC Announces Enforcement Task Force Focused on Climate and ESG Issues (Mar. 4, 2021), <https://www.sec.gov/news/press-release/2021-42>.

⁴⁹ Gary Gensler, SEC Chair, Statement Before the Financial Stability Oversight Council (Oct. 21, 2021), <https://www.sec.gov/news/public-statement/gensler-statement-financial-stability-oversight-council-102121>.

⁵⁰ *Id.*; see also Allison Herren Lee, Acting SEC Chair, Public Input Welcomed on Climate Change Disclosures (Mar. 15, 2021), <https://www.sec.gov/news/public-statement/lee-climate-change-disclosures>.

staff to provide recommendations regarding “governance, strategy, and risk management related to climate risk,” along with “specific metrics, such as greenhouse gas emissions, to determine which are most relevant to investors.”⁵¹ He has also requested “staff to consider potential requirements for companies that have made forward-looking climate commitments, or that have significant operations in jurisdictions with national requirements to achieve specific, climate-related targets.”⁵² The Commission has also sought public comments and input on proposed climate change disclosure rules.⁵³ Notably, proposed rulemaking concerning climate risk disclosure was included as a rulemaking priority on the SEC’s annual regulatory agenda released June 11 of 2021.⁵⁴ To date, the SEC has not indicated a date when a proposed rule will be released.

- Funds:

In an effort to tamp down on the practice of so-called “greenwashing,” the SEC is working to update naming rules for funds that seek to market themselves as “sustainable” and “green” and enhance required disclosures “so that investors can see what data, methodologies, and criteria stand between these names and claims.”⁵⁵ Rules relating to investment companies and investment advisers to address matters relating to ESG and fund naming rules also appear on the list of rulemaking priorities issued by the SEC.⁵⁶ The Division of Examinations also focused on ESG issues relating to funds in 2021, issuing a risk alert warning investors of various deficiencies and internal control weaknesses related to ESG investing that it had uncovered in its review of investment companies and funds’ ESG products and services.⁵⁷

While proposed rules have not been issued relating to either public companies’ disclosures or private funds, SEC staff has remained active in both areas, with the Division of Corporation Finance releasing a sample comment letter to companies highlighting issues that the Commission is expected to focus on in filings,⁵⁸ and the Asset Management Advisory and Investor Advisory Committees releasing recommendations for ESG disclosures.⁵⁹ Depending on how these rulemaking processes play out over the next year, companies may soon be required to make detailed uniform disclosures in their SEC filings relating to ESG, and private funds may face enhanced scrutiny relating to their naming and marketing practices concerning ESG issues.

2021 Enforcement

While the SEC did not commence any enforcement actions under these ESG initiatives in 2021, it is clear that the Enforcement Division is conducting investigative activity in the ESG space as certain ongoing enforcement investigations have been reported in the press, including an investigation into Deutsche Bank’s asset management arm regarding alleged overstatement of its use

⁵¹ Gary Gensler, SEC Chair, Remarks at London City Week (Jun. 23, 2021), <https://www.sec.gov/news/speech/gensler-speech-london-city-week-062321>.

⁵² *Id.*

⁵³ Allison Herren Lee, Acting SEC Chair, Public Input Welcomed on Climate Change Disclosures (Mar. 15, 2021), <https://www.sec.gov/news/public-statement/lee-climate-change-disclosures>. For further discussion of these issues, see Paul Weiss Publication, Acting SEC Chair Lee Discusses Additional Climate and ESG Initiatives (Mar. 17, 2021), <https://www.paulweiss.com/practices/transactional/capital-markets/publications/acting-sec-chair-lee-discusses-additional-climate-and-esg-initiatives?id=39582>.

⁵⁴ SEC Press Release, SEC Announces Annual Regulatory Agenda (Jun. 11, 2021), <https://www.sec.gov/news/press-release/2021-99>.

⁵⁵ Gary Gensler, SEC Chair, Statement Before the Financial Stability Oversight Council (Oct. 21, 2021), <https://www.sec.gov/news/public-statement/gensler-statement-financial-stability-oversight-council-102121>.

⁵⁶ SEC Press Release, SEC Announces Annual Regulatory Agenda (Jun. 11, 2021), <https://www.sec.gov/news/press-release/2021-99>.

⁵⁷ See Risk Alert, The Division of Examinations’ Review of ESG Investing (Apr. 9, 2021), <https://www.sec.gov/files/esg-risk-alert.pdf>.

⁵⁸ SEC Division of Corporation Finance, Sample Letter to Companies Regarding Climate Change Disclosures (Sept. 22, 2021), <https://www.sec.gov/corpfin/sample-letter-climate-change-disclosures>. For further discussion of these issues, see Paul Weiss Publication, SEC Division of Corporation Finance Publishes Sample Climate Disclosure Comments (Sept. 24, 2021), <https://www.paulweiss.com/practices/transactional/capital-markets/publications/sec-division-of-corporation-finance-publishes-sample-climate-disclosure-comments?id=41191>.

⁵⁹ SEC Asset Management Advisory Committee, Recommendations for ESG (July 7, 2021), <https://www.sec.gov/files/amac-recommendations-esg-subcommittee-070721.pdf>; SEC Investor Advisory Committee, Recommendation of the SEC Investor Advisory Committee Relating to ESG Disclosure (May 21, 2021), <https://www.sec.gov/spotlight/investor-advisory-committee-2012/esg-disclosure.pdf>.

of sustainable investing criteria to manage its portfolio and an investigation into Activision’s disclosures relating to allegedly pervasive issues of harassment and discrimination at the company.⁶⁰

Looking ahead, we anticipate that in 2022 the SEC will continue to work towards publishing final rules related to public companies’ climate and ESG-related disclosures and private funds’ naming conventions, and continue to commit resources in the Enforcement Division to investigate public companies relating to their climate and ESG-related disclosures and private funds for suspected “greenwashing.”

Additional Observations and Trends Detected in 2021 SEC Enforcement Activity

Overall enforcement numbers were down in 2021 – the SEC brought 697 enforcement actions in 2021, compared to 715 in 2020.⁶¹ That said, it is widely expected that under the new leadership regime those numbers will go up in 2022. Below we highlight some of the other trends we saw in 2021 enforcement activity and discuss what that might foretell for 2022.

Insider Trading

SEC enforcement activity and proposed rulemaking in 2021 shows that even if the number of insider trading cases has declined from its high water mark several years ago, it continues to be an important area of focus for the SEC. In 2021, the SEC pursued enforcement actions presenting novel legal theories against new and different actors than have typically been charged in the past. Among other such matters, the SEC brought: its first insider trading case involving the “dark web”;⁶² an action alleging insider trading for so-called “shadow trading,” where the accused had no material nonpublic information (“MNPI”) about the security in which he traded but instead allegedly possessed MNPI about another similar company;⁶³ and an action against a public company alleging a failure to maintain adequate internal controls under Section 13(b)(2)(B) where, among other things, the company allegedly failed to take adequate steps to ensure its insider trading policy was followed.⁶⁴ Much like in cryptocurrency and other areas, the SEC’s untested insider trading positions have resulted in an uptick in litigated cases.

The SEC is also proposing rule-based restrictions on insider trading. As has been widely reported, in December 2021, the SEC published proposed amendments to the 10b5-1 rules governing insider trading plans and proposed rules governing disclosures related to share buybacks.⁶⁵

Disclosure of Cybersecurity Breaches

In 2021, the SEC pursued significant investigations and brought several enforcement actions stemming from alleged failures to maintain controls sufficient to prevent cyber breaches and/or failures to disclose such breaches. In August 2021, the SEC announced that eight broker-dealers and/or investment advisers resolved enforcement actions arising from failures to prevent cyber-attacks that resulted in the exposure of personally identifying information of customers and clients.⁶⁶ The SEC also

⁶⁰ Patricia Kowsmann, Corinne Ramey, Dave Michaels, *U.S. Authorities Probing Deutsche Bank’s DWS Over Sustainability Claims*, WALL ST. J. (Aug. 25, 2021), <https://www.wsj.com/articles/u-s-authorities-probing-deutsche-banks-dws-over-sustainability-claims-11629923018>; Kirsten Grind & Sarah E. Needleman, *SEC is Investigating Activision Blizzard Over Workplace Practices, Disclosures*, WALL ST. J. (Sept. 20, 2021), <https://www.wsj.com/articles/sec-is-investigating-activision-blizzard-over-workplace-practices-disclosures-11632165080>.

⁶¹ SEC, Enforcement Results for Fiscal Year 2021 (Nov. 18, 2021), <https://www.sec.gov/files/2021-238-addendum.pdf>.

⁶² *SEC v. Apostolos Trovias*, No. 1:21-cv-05925 (S.D.N.Y. July 9, 2021).

⁶³ *SEC v. Matthew Panuwat*, No. 4:21-cv-06322 (N.D. Cal. Aug. 17, 2021). On January 14, 2022, the court denied the defendant’s motion to dismiss for failure to state a claim, holding that confidential information about the acquisition of one company could be material to investors in another company uninvolved in the acquisition and that trading on such information could be a breach of an executive’s fiduciary duty to his employer under the terms of the company’s insider trading policy.

⁶⁴ *SEC v. Cavco Indus., Inc.*, No. 2:21-cv-01507 (D. Ariz. Sept. 2, 2021).

⁶⁵ SEC Press Release, SEC Announces Enforcement Results for FY2021 (Nov. 18, 2021), <https://www.sec.gov/news/press-release/2021-238>.

⁶⁶ SEC Press Release, SEC Announces Three Actions Charging Deficient Cybersecurity Procedures (Aug. 30, 2021), <https://www.sec.gov/news/press-release/2021-169>.

charged multiple public companies in 2021 for failure to adequately disclose cyber incidents.⁶⁷ Beginning in June 2021 and continuing later in the year, the SEC sent letters to numerous public companies requesting information to assess whether they had been “impacted by the SolarWinds Compromise” and if so whether they had, among other things, made adequate disclosures of any such cyber breach.⁶⁸

The Enforcement Division’s focus on cybersecurity issues, in particular internal controls and disclosure issues, is likely to continue in 2022 as cybersecurity attacks continue to occur throughout the country and abroad.

Recordkeeping Requirements Relating to Personal Communication Devices and Messaging Platforms

With the proliferation and accessibility of technology and the decreasing barriers during the COVID pandemic between work and home, the SEC is investigating whether financial institutions and broker dealers are adequately maintaining relevant communications sent via personal devices and messaging platforms. In one recent and highly publicized enforcement action, the SEC settled with JPMorgan for failing to maintain potentially relevant employees’ communications sent on personal devices, including through text messaging, WhatsApp, and personal email accounts.⁶⁹ The SEC alleged that these records were not preserved, as required by securities laws, and that this was a well-known practice within the company, with senior leadership also using their personal devices for securities-related communications.⁷⁰ Press reports indicate that the SEC is investigating other financial institutions and broker dealers regarding retention of such communications; we expect this to continue to be an area of focus for the Enforcement Division for the foreseeable future.⁷¹

Looking Forward to 2022

Looking ahead to 2022, we expect to see a busy year of rulemaking and enforcement activity with particular attention paid by the Enforcement Division to matters involving, among other things, cryptocurrency; SPAC transactions; ESG disclosure issues; cybersecurity disclosure and internal control issues; and the use and retention of communications over personal devices and messaging platforms by financial institutions and broker dealers. As a result of untested legal positions being staked out by the Commission with respect to cryptocurrency, insider trading, and other areas, we also expect to see a continued rise in contested litigation with the Commission.

We also expect the SEC under Chair Gensler to continue to identify in 2022 additional areas for increased rulemaking and potential enforcement activity. For example, the SEC has very recently announced plans to require more private companies to engage in routine financial reporting that is already required of public companies.⁷² While discussions around these plans are in their early stages, these reporting requirements would likely be limited to so-called “unicorns,” large private companies valued at \$1 billion or more.⁷³ As the number of such high-value private companies continues to grow – there were 959 such

⁶⁷ See *In the Matter of First American Financial Corporation*, Order Instituting Cease-and-Desist Proceedings Pursuant to Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order, Exchange Act Rel. No. 92176, Admin. Proc. File No. 3-20367 (June 14, 2021), <https://www.sec.gov/litigation/admin/2021/34-92176.pdf>; *In the Matter of Pearson plc*, Order Instituting Cease-and-Desist Proceedings, Pursuant to Section 8A of the Securities Act of 1933 and Section 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order, Sec. Act. Rel. No. 10963, Exchange Act Rel. No. 92676, Admin. Proc. File No. 3-20462 (Aug. 16, 2021), <https://www.sec.gov/litigation/admin/2021/33-10963.pdf>.

⁶⁸ Katanga Johnson, U.S. SEC probing SolarWinds clients over cyber breach disclosures – sources, Reuters (June 22, 2021), <https://www.reuters.com/technology/us-sec-official-says-agency-has-begun-probe-cyber-breach-by-solarwinds-2021-06-21/>.

⁶⁹ *In the Matter of J.P. Morgan Securities LLC*, Order Instituting Administrative and Cease-and-Desist Proceedings Pursuant to Sections 15(b) and 21C of the Securities Exchange Act of 1934, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order, Exchange Act Rel. No. 93807, Admin. Proc. File No. 3-20681 (Dec. 17, 2021), <https://www.sec.gov/litigation/admin/2021/34-93807.pdf>.

⁷⁰ *Id.*

⁷¹ Dave Michaels, *JPMorgan Fined \$200 Million Over Employees’ Use of WhatsApp and Other Messaging Apps*, WALL ST. J. (Dec. 17, 2021), <https://www.wsj.com/articles/jpmorgan-admits-widespread-record-keeping-breakdown-in-sec-settlement-11639747801>.

⁷² Paul Kiernan, *SEC Pushes for More Transparency From Private Companies*, WALL ST. J. (Jan. 10, 2022), <https://www.wsj.com/articles/sec-pushes-for-more-transparency-from-private-companies-11641752489>.

⁷³ *Id.*

companies as of early January 2022, compared with 513 at the end of 2020⁷⁴ – the SEC’s regulatory and enforcement efforts in this space are likely to expand as well.

Alternative data is another area of potential enforcement activity that will be worth monitoring in 2022. In September 2021, the SEC announced the first ever enforcement action against an alternative data provider for allegedly misleading traders by failing to adequately disclose how it generated app performance data.⁷⁵ This action is not only relevant to vendors that aggregate and provide data that is not included in a company’s financial statements or other traditional data sources, but also has potential implications for trading firms that rely on alternative data and even the public companies that provide data to such vendors. Future enforcement activity in this area could focus on, among other things, whether trading firms are taking adequate measures to protect against misuse of alternative data and whether public companies are taking sufficient steps to try and ensure that vendors do not use the company’s data for improper purposes.

Chair Gensler has indicated that other significant areas of potential rulemaking in 2022 include rules curtailing or even banning payment for order flow⁷⁶ and rules to “freshen up” the equity market structure to “reflect today’s technology.”⁷⁷

These will be only some of the issues to keep an eye on in 2022.

We look forward to providing you with further updates on these and other developments in 2022.

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⁷⁴ *Id.*

⁷⁵ See In the Matter of App Annie Inc. and Bertrand Schmitt, Order Instituting Cease-and-Desist Proceedings Pursuant to Section 21c of the Securities Exchange Act of 1934, Making Findings, and Imposing Remedial Sanctions and a Cease-and-Desist Order Administrative Proceeding File No. 3-20549, Litigation Release No. 93975 (Sept. 14, 2021), <https://www.sec.gov/litigation/admin/2021/34-92975.pdf>.

⁷⁶ See Avi Salzman, *SEC’s Gary Gensler Has a Big, New Vision for the Stock Market. There Are Too Many ‘Inherent Conflicts of Interest’*, BARRON’S (Sept. 3, 2021), https://www.barrons.com/articles/sec-chief-gary-gensler-stock-market-51630626032?mod=hp_LEAD_2.

⁷⁷ See Gary Gensler, SEC Chair, Prepared Remarks at the Global Exchange and FinTech Conference (June 9, 2021), <https://www.sec.gov/news/speech/gensler-global-exchange-fintech-2021-06-09>.

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:

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