Behind the Numbers: Reviewing the SEC's Claim of a Record-Breaking Year

November 17, 2016 Kit Addleman, Carrington Giammittorio

The U.S. Securities and Exchange Commission reported a new single year high for enforcement actions in fiscal year 2016, filing a record 868 actions. Although this number is a significant jump from the previous two years, the total amount of penalties and disgorgements ordered is lower than in previous years. Additionally, a large number of the tallied enforcement actions were the result of sweep investigations that leveraged staff resources to generate multiple actions out of a self-reporting program, such as the SEC's Municipalities Continuing Disclosure Cooperation Initiative, or numerous actions out of a single investigation such as the F-Squared Investments matter involving 13 advisers who were alleged to have repeated misleading performance data. But Fiscal Year 2016 did see an increased emphasis on whistleblower protections, with a record $57 million being awarded to whistleblowers, as well as the first stand-alone action for retaliation against a whistleblower.

In terms of the sheer number of total actions, 2016 was a record year for the Commission. The SEC filed a total of 868 enforcement actions, 548 of which were stand-alone or independent actions.[1] Along with 195 follow-on administrative proceedings and 125 delinquent filings violations, these actions resulted in $4 billion in disgorgements and penalties.[2]

The SEC's "Broken Windows Initiative," a program to punish smaller, technical violations in an effort to stop potentially larger future wrongdoing before it occurs, is clearly demonstrated by dozens of actions in the 2016 results. It is unclear whether actions involving technical missteps are effective in protecting investors. But, it is clear that counting a smaller "broken windows" action as equivalent to a larger market fraud or pervasive intentional misconduct is a poor measure of the SEC's enforcement program.

The SEC touted the following as its most significant enforcement actions:

- A $415 million enforcement action against a leading broker/dealer for violating customer protection rules;
- A $267 million enforcement action against a major international bank's wealth management subsidies for failing to disclose conflicts of interest;
- Insider trading charges against a hedge fund manager as well as a sports gambler and his alleged source, a former public company board member; and
- CPA cases against the Och-Ziff hedge fund and its CEO and CFO as well as VimpelCom Ltd., resulting in settlements of hundreds of millions of dollars.

Despite the record-breaking number of total filings and stand-alone actions, the SEC ordered just over $4 billion in penalties and disgorgements; down from $4.19 billion in 2015 and $4.16 billion in 2014.

The dip in disgorgements and penalties likely is a result of the SEC's focus on smaller violations and an increase in self-reporting. For example, under the Municipalities Continuing Disclosure Cooperation ("MCDC") Initiative launched in March 2014, the Enforcement Division announced that it would recommend "standardized, favorable settlement terms" to municipal issuers and underwriters who self-report having made inaccurate statements in bond offerings.[3] Of the 868 enforcement actions filed by the Commission in 2016, 85 were the result of self-reporting through this initiative.[4] (See our recent coverage here). And while ten of 36 underwriters paid the maximum $500,000 penalty in the first round of settlements under that initiative, only one firm was assessed the maximum penalty in the second round. (See our coverage of those settlements here and here).

But fiscal year 2016 *has* seen an increased focus on rewarding whistleblowers and halting retaliation against whistleblowers. Over $57 million was awarded to 13 whistleblowers in 2016—more than in all previous years combined.[5] The SEC also brought its first stand-alone action for retaliation against a whistleblower.[6]

The Commission's year-end numbers – both the increase in total actions and the dip in recoveries – should be no surprise given its focus on self-reporting, prosecution of arguably smaller technical violations, use of data analytics to uncover fraud, and pursuit of first-of-their kind cases. While it is uncertain how the presidential results and potential changes to commissioners may impact the enforcement program in the longer term, market participants and public companies should anticipate that the current trends in enforcement will continue through the first part of the SEC's 2017 fiscal year.

For more information contact one the lawyers listed below.

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[1] *See* Press Release, SEC Announces Enforcement Results for FY 2016 (Oct. 11, 2016).

[2] *Id.*

[3] *See* Press Release, SEC Launches Enforcement Cooperation Initiative for Municipal Issuers and Underwriters (Mar. 10, 2014).

[4] *Id.*

[5] *See* Press Release, SEC Announces Enforcement Results for FY 2016 (Oct. 11, 2016).

[6] *See* Press Release, SEC: Casino-Gaming Company Retaliated Against Whistleblower (Sep. 29, 2016).