

# Financial Regulation & Risk

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## Q&A 'No Fish Too Small' in the SEC's Focus on Individual Cases, Say Former Prosecutors



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- The Securities and Exchange Commission's focus on smaller issues is a "megatrend."
- The SEC has become more sophisticated in its investigations.
- Enforcement focus is likely to remain unchanged regardless of the U.S. election result.
- Regulated firms need to document their processes.

Interview by Ayesha Javed, Bloomberg Briefs. Comments were edited and condensed for clarity.

#### Q: What types of client regulatory issues do you deal with most?

**CC:** There has been a lot of public commentary about the focus on individuals. The Yates memo, coming out of the U.S. Department of Justice, has spurred and caused a lot of attention on the potential liability of individuals. Also, there were a series of cases over the last couple of years in which the SEC named chief compliance officers as individuals to be named in enforcement proceedings. There's no question that the Yates memo has focused attention and brought some structure to the way the Department of Justice pursues individuals and because of that the SEC as well. But as a practitioner — and based on my experience when I was at the commission — there truly has always been a focus on individuals and a desire on the part of prosecutors to pursue cases against individuals.

**HS:** What's different in today's environment is the political pressure. That all the noise out there is calling for individuals. One of the megatrends I see is the commission is prosecuting smaller and smaller matters and, in a sense, really bullying the client in a way that is sort of a low point in the history of the commission. There's no fish too small not to throw back.

#### Q: Could regulators therefore be missing worse misconduct?

**HS:** The SEC's big problem is to be current. They're always working on yesterday's news. So they're working on CMO and CDOs when that problem has long since passed. Their allocation error is that that they're spending too many assets on historical problems — some of which aren't that significant — and aren't

involved in the current new problem. Part of the problem with the commission is their black eye on [Bernard] Madoff. They looked at something and missed the big picture. So one of their problems, which is causing the misallocation of resources, is that they're terribly afraid of looking at something but not diving deep enough to have seen if there's a really big problem.

#### Q: How could the SEC be more forward-looking?

**CC:** They continue to leverage technology and automation to identify practices and concerns that are troubling to them. The problem with that is technology is changing so fast, and in a market where people have even greater incentive to have better technology than the SEC does, they're always going to be stuck a little bit behind.

**HS:** Backlog is a big issue. They have cases which are three, four, five years old — they can't just fish or cut bait off of them. The backlog is what's sucking up too many resources, so they can't get current. The commission has been on a straight line going up, to have resources so that there are people that both understand the marketplace and the technology. So they have vastly improved on that level. We often lecture our clients that the SEC's level of sophistication has become much greater. Their ability to track trades, follow trades, analyze the trading data and their automation is significantly improving. We often tell clients they need to realize that that change has occurred.

#### Q: How do you expect the U.S. election result to affect enforcement?

**CC:** The thing I like about what I do is that whether it's in a Republican-controlled

or a Democratically-controlled Congress, there's always been an incentive and pressure on the enforcers to be more aggressive and I don't think that's going to change. Whether it's the Republican-slash-populist nominee [Donald Trump] who has built his entire record on his populism, at least through the course of this campaign, I think he will view that as a justification for being very aggressive in terms of enforcement. On the Democratic side, particularly with the role that [Senator] Elizabeth Warren might play in a future administration and her leanings, I think we are in for a period of even greater focus on white-collar crime, and on securities enforcement of all sorts.

**HS:** The SEC has historically been an independent agency which has pursued the agenda that it feels appropriately, without tremendous impact from the executive branch. So I think that it will continue to be an effective enforcer regardless of who is elected. Obviously if [Hillary] Clinton is elected I think the more liberal side of the party will continue to mount political pressure for a more regulated environment and if Congress passes more regulations, the SEC will enforce them. I think the enforcement agenda has been and will continue to be relatively politics-free.

#### Q: How should firms prepare?

**HS:** I tell clients this is a really bad time to be in trouble. The other thing is that process has taken on more importance over substance. So the fact that you didn't intend to do something wrong isn't sufficient. You have to have a process in place and you have to document that.