



## SEC Enforcement Trends: Five Key Takeaways

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The U.S. Securities and Exchange Commission **recently announced** its enforcement results for FY21, highlighting what it considers significant in its enforcement practices and indicating important trends for future enforcement. The data from FY21 suggest that this new SEC will pursue an aggressive enforcement agenda, continue to impose—and even raise—significant penalties, and test the waters with first-in-kind cases.

### 1. A Close Look at FY21 Enforcement Metrics Suggests Aggressive Enforcement in FY22

While the SEC brought fewer total enforcement actions in FY21, the 3 percent decrease in the number of enforcement actions compared to FY20 does not reflect a decline in the SEC's appetite for enforcement. The SEC emphasized in its announcement that the number of **new enforcement** actions in FY21 increased **7 percent** over FY20.

The number of enforcement actions against public companies in FY21 was down, but this is not likely to continue. With only 53 total public company actions during FY21, this represents a **15 percent decrease** from FY20 and represents the lowest number of public company enforcement actions since FY14. However, some of the decrease in public company actions may be attributed to the ongoing effects of the COVID-19 pandemic and to the new chairman's transition. NYU and Cornerstone Research, which track data on SEC enforcement, **noted in their analysis** of the SEC's announcement that actions have historically decreased in years when a new chair has been sworn in.

The decrease in enforcement actions, including those against public companies, is not likely to persist. Chair Gensler, in **remarks at the Securities Enforcement Forum** in November, emphasized the importance of taking "high-impact cases" to "change behavior" and send a message to the rest of the market.

### 2. Expect the SEC to Maintain Focus on Gatekeepers and Individuals

While the SEC described a broad range of enforcement areas in its press release, its first two listed targets follow long-term priorities: ensuring that gatekeepers of the securities markets, such

as attorneys and auditors, live up to their obligations; and holding individuals accountable for their actions.

In a [speech](#) at The Practising Law Institute's SEC Speaks in October 2021, Director Grewal emphasized gatekeeper accountability as one of the primary ways to ensure public trust in the capital markets. The SEC highlighted key enforcement actions in this area in its annual statement, including bringing administrative proceedings [against an audit partner](#) for improper professional conduct during an audit; [barring an attorney](#) from appearing or practicing before the SEC for fraudulently facilitating an offering; and bringing an administrative proceeding [against a CPA](#) for failing to register with the Public Company Accounting Oversight Board and for multiple failures in the audit process.

According to Director Grewal, lawyers and auditors are often the “first lines of defense” against misconduct in the markets, so we can expect that the Enforcement Division will continue to maintain a “significant focus” on these gatekeepers in the coming year.

Director Grewal also highlighted accountability of individuals and the importance of tailoring remedies to keep bad actors out of the capital markets. At SEC Speaks, he described officer and director bars as a “critical tool” in preventing further misconduct. If an individual has violated the securities laws, the SEC will think carefully about whether that individual could later be in a position in a public company and continue to harm investors, and impose a bar if necessary. Across the board, the SEC is looking closely at individual conduct and will likely continue to do so next year. In FY21, **70 percent of new enforcement actions involved at least one individual defendant or respondent.**

### 3. Expect Higher Penalties

Enforcement methods also shifted significantly in FY21. While the total amount of disgorgement judgments and orders (\$2.4 billion) declined 33 percent from FY20, total penalty amounts obtained **increased 33 percent** from the prior year. Following the [Supreme Court's decision](#) in *Liu* last year, which limited disgorgement to a wrongdoer's net profits, a reduction in disgorgement amounts comes as no surprise.

The increase in penalties, however, may reflect more than *Liu's* limitation on disgorgement as a remedy: it may also signal the beginning of a new approach within the SEC with respect to both the amount of penalties assessed and the justification for seeking penalties. Earlier this year, in a [speech](#) to the Council of Institutional Investors, Commissioner Caroline Crenshaw stated that the SEC should focus more on the egregiousness of the wrongdoer's conduct than the impact to shareholders when assessing penalties. In her view, penalties should be higher for violations that cause more harm, either on their own or in the aggregate when considering their frequency as well as for violations that are difficult to detect. She also argues that engaging in an analysis of whether a corporation's shareholders benefited from misconduct or how a penalty may harm shareholders, which has generally tempered large penalties, leads to a “myopic approach” that should be eschewed.

Director Grewal also stated in [recent remarks](#) that while “penalties levied in the past are certainly a relevant data point,” historic penalties will not be the “beginning and end of [the SEC's] analysis” when thinking about deterring conduct in future enforcement actions. According to

Director Grewal, even first-time offenders could face significant penalties if they engage in conduct for which the SEC has penalized other actors. In short, this increase in penalties is likely just the beginning of the SEC's new approach to deterrence.

#### 4. The Rise of “First-in-Kind” Cases Will Continue . . . and So May Litigation

In its press release, the Commission highlighted some of its “first-of-their-kind” cases in a wide range of areas, which Director Grewal anticipates will “lead to even more successful actions in the future.”

One example of the SEC pushing the envelope and testing new theories of fraud in court is its August 2021 filing of insider trading charges against a former employee of a pharmaceutical company when he allegedly traded in *another* company's options based upon confidential information about his *own* employer. In another first enforcement action of its kind, in September 2021, the SEC reached a \$10 million settlement with an “alternative data” provider for misrepresenting how its data was sourced and used and then encouraging its securities trader customers to rely on the improperly obtained data to estimate market performance.

The SEC has sent a message to market participants that it is thinking creatively to enforce the federal securities laws. And although many respondents may feel they have little choice other than to settle with the SEC, those who do choose to litigate may find the courts receptive to arguments that challenge inventive agency actions.

#### 5. This Is the Heyday of the Whistleblower

This year, the SEC's whistleblower program passed a total of **\$1 billion** in awards since it began in 2011, with over **\$564 million** of that total coming in the last fiscal year alone. **Four of the highest-ever** SEC whistleblower awards were given in FY21, with a **\$36 million award** given to a whistleblower who was culpable in the wrongful conduct and delayed reporting. Whistleblower tips to the Commission also skyrocketed: the SEC received **12,210 tips in FY21**, a **76 percent increase** over the prior fiscal year which represents **nearly a quarter of all tips since the beginning of the program**.

The Whistleblower Program's 2021 Annual Report **noted** that 75 percent of award recipients who were insiders of the reported entity had *already* raised their concerns internally before reporting them to the SEC. Given the SEC's appetite for increased enforcement and the large rise in tips and awards this year, companies should carefully assess their internal reporting mechanisms to ensure they can detect wrongdoing, encourage tipsters to report within the entity, and proactively address the problems.

The SEC's Whistleblower Rules were **amended in 2020** to increase efficiency in the tip review process, make it easier for whistleblowers to report to the Commission, and give whistleblowers a presumption of the statutory maximum award for certain awards of \$5 million or less. While it may be too early to say what impact the amendments have had so far, the numbers indicate that the Commission is looking closely at whistleblower tips and is sending a strong message to the public and to market participants that it is ready to act on information it receives about potential misconduct and reward those who share it.

## Conclusion

Between an increasing appetite for aggressive enforcement and the offer of huge rewards for whistleblowers, the Commission's drop in overall cases in FY21 will not likely continue in the coming year. With the SEC thinking strategically and creatively about how to enforce the securities laws and protect investors, public companies and registrants should carefully assess their compliance and whistleblower response programs.