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PUBLIC COMPANY UPDATE

Changes Continue in SEC Enforcement: New Initiative to Encourage Cooperation by Individuals

As a part of its continuing effort to revamp and energize its Enforcement Division, the Securities and Exchange Commission (SEC) unveiled new tools to encourage cooperation by individuals and companies during investigations.

For nearly a decade, companies have been able to determine whether and to what extent they will get credit for their cooperation in an investigation by referring to the so-called “Seabord Report,” which outlines the principles considered when evaluating cooperation by companies.¹ The SEC has now declared that it will apply similar factors to evaluate whether, how much and in what manner to credit cooperation by individuals. The goal is to provide an incentive for employees, officers, directors and even third parties to report violations and cooperate fully and promptly in enforcement matters. Those credited with cooperation may be able to reduce or even avoid the charges they might otherwise face.

The guidance the SEC issued last week identifies four general considerations for assessing an individual’s cooperation with the Enforcement staff:

- The assistance provided by the cooperating individual;
- The importance of the underlying matter in which the individual cooperated;
- The societal interest in ensuring the individual is held accountable for his or her misconduct; and
- The appropriateness of cooperation credit based upon the risk profile of the cooperating individual.

In addition to the availability of reduced sanctions or penalties to reward cooperation, the SEC is providing its Enforcement staff with some new tools similar to those that have long been available to criminal prosecutors, but which have never been used in the SEC-initiated civil proceedings. These devices can be used for cooperating individuals or companies:

- ***Cooperation agreements.*** Formal written agreements in which the Enforcement Division agrees to recommend to the SEC that a cooperator receive credit for cooperating in investigations or related enforcement actions if the cooperator provides substantial assistance, such as full and truthful information and testimony.
- ***Deferred prosecution agreements.*** Formal written agreements in which the SEC agrees to forego an enforcement action against a cooperator if the individual or company agrees, among

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other things, to cooperate fully and truthfully and to comply with express prohibitions and undertakings during a period of deferred prosecution.

- ***Non-prosecution agreements.*** Formal written agreements, entered into under limited and appropriate circumstances, in which the SEC agrees not to pursue an enforcement action against a cooperator if the individual or company agrees, among other things, to cooperate fully and truthfully and comply with express undertakings.

The SEC is looking to the Department of Justice (DOJ) and criminal prosecutions for guidance on how to use these tools.² One important distinction, however, is that DOJ prosecutors have the discretion to use these tools as they see fit. In the SEC context, however, Enforcement staff can only make a recommendation to accept a cooperation agreement. The SEC can ignore the cooperation and reject the Enforcement Division's recommendation for a lesser sanction against the cooperating individual.

The cooperation of individual witnesses has long been important to the SEC's ability to bring enforcement cases against companies and individuals. While it remains to be seen how the Enforcement staff will use these new tools, their availability gives the SEC additional means of encouraging individuals to report wrongdoing and to provide complete and honest information.

FOR MORE INFORMATION

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¹ Available at: <http://www.sec.gov/litigation/investreport/34-44969.htm>.

² In addition, although the SEC's announcement on this cooperation program uses the word "prosecution" (which is normally associated with criminal proceedings), the SEC only has the authority to bring civil actions. The SEC can, however, make referrals to the DOJ where it believes a criminal investigation is warranted.