

Clients & Friends Memo

New Enforcement Director Outlines Priorities for “Robust” Enforcement at SEC

December 16, 2021

On December 15, 2021, the D.C. Bar hosted a one-hour conversation with Gurbir S. Grewal, the SEC’s new enforcement director. Mr. Grewal spoke about his prosecutorial background and preparedness to lead the agency’s Division of Enforcement, as well as his top priorities.

Prosecutorial Background

Mr. Grewal joined the SEC this year after a distinguished career as a prosecutor, including his service as an Assistant United States Attorney in New Jersey and Brooklyn, and as New Jersey’s Attorney General. He dismissed concerns that some have expressed about a former prosecutor leading an agency that has only civil and regulatory authority. Whether prosecuting crimes or enforcing rules in civil litigation, the goal is to administer justice and uphold the rule of law, he said. That said, he added that he plans to approach SEC enforcement with a “prosecutor’s mindset” in pursuing facts and perceived violations of law. Leading a staff of 8,000 in the New Jersey Attorney General’s office taught him to manage resources to match his goals, he said, noting that “if you make everything a priority, then nothing is a priority.” He stated that he plans to adopt the same approach to SEC enforcement, streamlining processes and matching resources to meet priorities.

Enforcement Priorities

Mr. Grewal echoed earlier public remarks and said that “restoring public trust” in financial markets is his overarching goal. To that end, he identified three tools to help him achieve that goal: (1) robust enforcement; (2) robust penalties; and (3) robust compliance.

- *Robust enforcement.* Mr. Grewal intends to approach enforcement with a “sense of urgency.” When it comes to the SEC’s broad mission of protecting public investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation, Mr. Grewal said that he intends to “cover the waterfront” by bringing appropriate cases and doing so with efficiency. Emerging trends will be a focus, and the Division of Enforcement will endeavor to stay ahead of issues, such as cryptocurrency, cybersecurity, ESG, and SPACs. Mr. Grewal noted that the SEC will be more willing to litigate cases where its enforcement interests are greatest, though appropriate consideration will be given to staff resources and litigation risks.

Mr. Grewal added that his sense of urgency will inform his decision whether he or his Deputy Director, Sanjay Wadhwa, attend “Wells” meetings (where companies may present their position regarding a potential securities violation, prior to an enforcement action). When a Wells request does not present a “novel” or “programmatic” issue for the SEC, he is unlikely to attend. He noted, however, that every decision undergoes multiple layers of review and that companies can expect him to review their submissions.

Speaking to cryptocurrency in particular, he asserted that the SEC has effectively dealt with emerging technologies in the past, and its approach to cryptocurrency will be no exception. He noted that the Howey test defining what products are securities and existing rules have endured and continue to provide industry guidance. The Division of Enforcement will ensure that its public-facing documents clearly articulate the bases for its actions, so that the public will be informed as the industry continues to develop. Though he did not provide any specific views on cryptocurrency, he noted that when it comes to so-called Decentralized Finance (DeFi) platforms, he does not place much stock in mere “labels,” adding that his view is that each product must be assessed based on its facts and circumstances. He noted that where one core group of individuals is responsible for coding and administering a platform, it is difficult to consider it “decentralized.”

- *Robust penalties.* Mr. Grewal said that appropriate penalties, particularly admissions of wrongdoing, send a message of accountability to the market and have a prophylactic effect. Not every case will require an admission, he was quick to point out, but in cases where the public interest is best served by acceptance of responsibility, admissions may be required. Such cases may include those in which a large number of investors are harmed or the conduct is particularly egregious or poses a significant risk to the market or the SEC’s mission. The Division will also consider whether an admission of wrongdoing would help an investor in deciding whether to deal with a party going forward.

In terms of financial penalties, Mr. Grewal said that the magnitude of penalties will continue to depend on the facts and circumstances of each violation, with greater penalties accruing to those who engage in repeat violations within the same firm or industry.

Mr. Grewal touched on cooperation credit and noted that this year marked the 20th anniversary of the Seabord Report in which the SEC articulated its framework for evaluating cooperation with its investigations. The factors that resonate with him are self-reporting and early disclosure—companies stand to gain the most when they self-report and “short-circuit” the SEC’s investigation by conducting their own robust investigation, presenting on what was discovered, addressing misconduct, and implementing a plan to prevent future misconduct. Merely going through the motions of what is “required” by responding to SEC subpoenas and producing witnesses is not enough to move the needle on cooperation, he said.

Mr. Grewal also addressed a trend of what he considers to be “serious” document preservation issues in investigations. Document preservation is more important than ever as work has shifted to remote environments, he cautioned. Where the SEC encounters instances where company personnel make the conscious decision to move communications offline or to ephemeral channels, he views that as a deliberate attempt to evade regulators. The SEC has sought spoliation instructions in cases where this has come up, a practice that should be expected to continue if spoliation is present.

- *Robust compliance.* Mr. Grewal hopes to foster an environment in which the SEC can work with compliance officers and other gatekeepers to ensure that employees operate within the rules. He said that companies should feel comfortable engaging with the SEC regarding their businesses and industries. He pointed to the SEC’s FinHub as one space for such dialogue. When asked if companies should be wary that what they tell the SEC may lead to an enforcement action, Mr. Grewal did not dismiss that risk. He said, however, that Enforcement will view a company that comes in to discuss its conduct more favorably than a company that does not.

Mr. Grewal’s comments continue the trend of tough talk from the SEC, often the norm upon the arrival of a new chair or enforcement chief and certainly since the arrival of Chairman Gensler. Since its failure to uncover the Madoff fraud until far too late, the enforcement division has since 2009 turned to a series of highly-decorated former federal prosecutors to serve as division director, turning away from the practice of promoting from within that had prevailed for decades dating back to the division’s creation in the 1970s. During their tenures as director, those former prosecutors have disfavored certain cases, like the accounting cases historically at the core of the enforcement program, in favor of others that might be said to have more headline and jury appeal, such as those involving cryptocurrencies and, even more so, insider trading cases. It remains to be seen what path Mr. Grewal will follow as enforcement director. And while his comments here certainly represent an aspirational list, attention should also be paid to the agency’s recent results in court, including a sobering directed verdict and midtrial loss in a particularly circumstantial insider trading case filed in the Eastern District of Virginia. We will be watching these results closely in the months ahead.

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If you have any questions, please feel free to contact any of the following Cadwalader attorneys.

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