Lowenstein Sandler

Client Alert

Investment Management

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SEC Division of Enforcement Announces 2018 Results

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On November 2, 2018, the U.S. Securities and Exchange Commission's Division of Enforcement (the Division) published its 2018 annual report (the Report), which details the Division's activities during fiscal year 2018.[1] The Report describes the Division's "many notable successes" and reiterates the Division's mission.

Overall, enforcement actions, disgorgement, and penalties increased modestly year over year. In total, the Division brought 821 actions, ordered $3.945 billion in disgorgement and penalties, and returned $794 million to harmed investors in FY 2018. This compares to 754, $3.789 billion, and $1.073 billion, respectively, in 2017.

Actions regarding securities offerings still comprise the highest percentage of the Division's enforcement actions at 25% (121 actions in FY 2018), and actions involving investment advisers or investment companies finished a close second at 22% (108 actions in FY 2018). Actions involving insider trading totaled 10% (51 actions in FY 2018). Notably, actions involving securities offerings and investment advisers or investment companies represented the largest increases in cases over 2017.

The Report also articulated the Division's five guiding principles:

- **Focus on the Main Street Investor.** The Division is focused on protecting the interests of retail investors, with particular attention paid to returning sums to harmed investors.
- **Focus on Individual Accountability.** The Division is focused on holding individuals accountable as a way to ensure that the institutions to which those individuals belong avoid wrongdoing.
- **Keep Pace with Technological Change.** The Division will continue to leverage its fully operational Cyber Unit, which investigates matters involving, among other things, cyber-crimes, cyber-security, and crypto-currencies.
- **Impose Remedies That Most Effectively Further Enforcement Goals.** The Division seeks to impose remedies that will both (i) punish wrongdoers and (ii) deter would-be wrongdoers.
- **Constantly Assess the Allocation of Our Resources.** The Division has reacted to decreases in resources in ways that allow it to maintain its activities and achieve its stated goals.

In addition to its guiding principles, the Division articulated a number of initiatives and explained its strategies for furthering those initiatives. For its *Focus on the Main Street Investor* initiative, the Division formed its Retail Strategy Task Force, which uses data analytics to identify wrongdoing in order to protect retail investors. For its *Policing Cyber-Related Misconduct* initiative, the Division's Cyber Unit focused on initial coin offerings, crypto-assets, and cyber-security risks. Finally, for its *Share Class Selection Disclosure Initiative*, the Division launched a voluntary program where investment advisers can self-report disclosure failures related to 12b-1 marketing and distribution fees paid by (mostly retail) advisory clients.

Finally, the Report also details the Division's actions taken in response to the resource constraints imposed on it over the past two years. Since 2016, the SEC has worked under an agency-wide hiring freeze, which has resulted in a 10% reduction in

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[1] The SEC's 2018 fiscal year ended September 30, 2018. The full text of the Report is available at https://www.sec.gov/files/enforcement-annual-report-2018.pdf.

headcount at the Division. Despite being budget constrained, the Division managed to increase its investigative and enforcement activities, so investment advisers should not assume that lower resources will lead to diminished activity.

While the current administration touts its achievements in reducing regulation across a variety of industries, the Report serves as an important reminder that the SEC remains an active and capable regulatory agency. In terms of the “Wall Street versus Main Street” narrative, Division Co-Directors Stephanie Avakian and Steven Peikin believe that the SEC can oversee both as stated in the Report as follows:

> “[W]e do not believe the Commission faces a binary choice between protecting Main Street and policing Wall Street. It must do both. In many cases … misconduct at these institutions causes substantial harm to investors on Main Street.
>
> This year, as the Division of Enforcement focused its lens on protecting Main Street investors, it continued to investigate and recommend actions against financial institutions, intermediaries, and other market participants.”[2]

Observations and Recommendations

As suggested in our February 2018 Client Alert,[3] the Division’s 2018 Report demonstrates that there was not a significant drop-off in either examinations or in the number of enforcement actions brought in 2018. In fact, given the increase in both the efficacy of the technology utilized by the SEC and the sophistication of its staff, the SEC appears to have embraced its "do more with less" mantra. We encourage investment advisers and other financial market participants to ignore the noise in the market about reduced regulation and remain vigilant in light of the Division’s active pursuit of enforcement actions in furtherance of its stated initiatives.

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[2] See Report at page 1.
[3] See https://www.lowenstein.com/news-insights/client-alerts/the-sec-s-2018-examination-priorities-investment-management-client-alert.

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