

## SEC Establishes Incentives for Individuals and Companies to Cooperate with Investigations and Enforcement Actions

On January 13, 2010, the Securities and Exchange Commission (the “Commission”) announced various initiatives to encourage individuals and companies to fully and truthfully cooperate with Commission investigations and enforcement actions.

### I. New Cooperation Tools

First, the Commission has authorized its Division of Enforcement to use several cooperation tools previously unavailable in securities enforcement cases, including cooperation agreements, deferred prosecution agreements, and non-prosecution agreements.

- **Cooperation Agreements.** A cooperation agreement is a formal written agreement between the Division of Enforcement and an individual or corporation (“cooperator”). As part of the cooperation agreement, the Division of Enforcement will agree to recommend that a cooperator that has provided substantial assistance receive credit from the Commission. The Commission, however, will still decide what, if any, credit to provide to a cooperator.
- **Deferred Prosecution Agreements.** A deferred prosecution agreement is a formal agreement between the Commission and a cooperator. As part of the deferred prosecution agreement, the Commission will agree to forego an enforcement action against a cooperator during the period of deferred prosecution if the cooperator agrees to (i) cooperate fully with the Commission’s investigation and (ii) comply with certain prohibitions and undertakings.
- **Non-Prosecution Agreements.** A non-prosecution agreement, which the Commission has indicated it will enter into under “limited and appropriate circumstances,” is a formal agreement between the Commission and a cooperator. As part of the non-prosecution agreement, the Commission will agree not to pursue an enforcement action against a cooperator if the cooperator agrees to (i) cooperate fully with the Commission’s investigation and (ii) comply with certain prohibitions and undertakings.

These cooperation tools have been regularly used by the Department of Justice in its criminal investigations and prosecutions and are designed to afford similar protections to cooperators in civil securities enforcement matters.

## **II. Witness Immunity Requests**

Second, the Commission has delegated to the Director of the Division of Enforcement the authority to make requests for witness immunity directly to the Department of Justice without first seeking an order from the Commission, thereby streamlining the process for submitting witness immunity requests. Before this change in policy, the Division of Enforcement lacked the authority to grant immunity to any witnesses without a Commission order and first receiving approval from the Attorney General.

## **III. Expansion of “Seaboard Report” to Individuals**

Third, the Commission has promulgated a new policy to evaluate cooperation provided by individuals. In 2001, the Commission’s “Seaboard Report” established a framework to assess whether a corporation should receive leniency as a reward for cooperation with an investigation. The framework in the Seaboard Report includes many factors built around four general principles: self-policing, self-reporting, remediation, and cooperation. Now, for the first time, the Commission provides an analogous framework for cooperation by individuals that it expects will provide an incentive for individuals to cooperate early and completely (the Department of Justice has for many years utilized a similar program in its enforcement of federal criminal laws).

Although the Commission’s jurisdiction is exclusively civil, as a reward for cooperation, it can decide to forego enforcement action or to pursue reduced charges and sanctions. To guide that decision with respect to individuals, the new policy articulates four main considerations (each with a number of specific sub-factors):

- Assistance provided by the individual (including its value, quality, nature, willingness, and timeliness);
- Importance of the underlying matter (including the type of securities involved, duration of any misconduct, danger to investors, amount and type of harm, and whether it was an SEC priority);
- Interest in holding the individual accountable (including the individual’s own culpability and whether actions were taken to prevent, mitigate, or remediate any harm); and
- Profile of the individual (including history of lawfulness, acceptance of responsibility, and the ability to commit future securities violations).

The Commission notes that this new policy creates no legally enforceable rights, the stated factors are non-exhaustive, the factors have no particular order of importance, and each factor may receive different weight depending upon the unique facts of each case. Despite the broad discretion retained by the Commission, a principal purpose of placing this policy in writing is to instill greater predictability and consistency in the Commission's treatment of cooperators. It will take some experience with the new policy to see whether the Commission can indeed apply it in a consistent manner.

#### IV. Conclusions

First, although these new initiatives provide the Division of Enforcement with new tools to promote cooperation in investigations, only time will tell how and under what circumstances the Division of Enforcement implements these initiatives. In August 2009, Robert Khuzami, the current Director of the Division of Enforcement, in outlining the then-proposed initiatives said he believed cooperators should be rewarded only when they provide "extraordinary cooperation."<sup>1</sup> Khuzami added, "While I believe in giving credit for cooperation that results in tangible benefits for investors and the Enforcement program, I don't believe in being lenient for the sake of leniency, or for rewarding persons for simply complying with routine or expected requests."<sup>2</sup> What constitutes "extraordinary" cooperation remains to be seen.

In addition, while these initiatives provide the Division of Enforcement with greater ability to negotiate with cooperators, the initiatives do not give the Division of Enforcement the authority to make final decisions regarding civil remedies without the approval of the Commission or potential criminal immunity without the approval of the Attorney General. As a result, the value of these initiatives will be largely determined by how the Commission and the Department of Justice react to the Division of Enforcement's recommendations.

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<sup>1</sup> Robert Khuzami, Director, SEC Division of Enforcement, Remarks Before the New York City Bar: My First 100 Days as Director of Enforcement (Aug. 5, 2009), *available at* <http://sec.gov/news/speech/2009/spch080509rk.htm>.

<sup>2</sup> *Id.*

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