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What a Difference a Year Makes: *Impact of Dodd-Frank Title IX*

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Title IX: Investor Protection and Securities Reform Act of 2010



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Part I:

The Impact of Title IX on SEC Enforcement Actions

*Giving the SEC more
(and sharper!)
tools for enforcement*



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Part I: The Impact of Title IX on SEC Enforcement Actions

- Nationwide Service of Subpoenas
- Civil Penalties for Administrative Proceedings
- Extraterritorial Jurisdiction
- Increased Risk to Multi-Sector Bans



Nationwide Service:

The SEC Will Find You Anywhere!

- Prior law only allowed subpoenas that would require travel of 100 miles or less
- Section 929E provides for nationwide service of subpoenas in actions brought by the SEC under the Securities Act, the Exchange Act, the Investment Company Act and the Investment Advisors Act
- Applies to the SEC as well as the Defendant



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Nationwide Service: The Impact

- SEC already had this power in administrative proceedings
- May lead to forum shopping to the extent the SEC can properly establish venue



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Extraterritorial Jurisdiction:

You Can't Do There What You Can't Do Here

- Overrides 2010 Supreme Court decision in *Morrison v. National Austrian Bank, Ltd.* by providing jurisdiction for transactions outside the United States which limited the antifraud provision of Exchange Act to “transactions in securities listed on domestic exchanges, and domestic transactions in other securities”
- Extends reach even if transactions occur outside the United States and only involve foreign investors



Extraterritorial Jurisdiction: The Impact

- Does not yet apply to private litigants
- Study underway to review the extent to which private rights of action would be available
 - Tone appears to be to move toward more explicit and implied private rights of action



Increased Penalties: Civil Penalties

- SEC may now seek civil penalties in administrative proceedings for violations
- Attractive Forum for the SEC
 - Limited discovery
 - No jury trial
 - Appeal is to SEC Commissioners



Increased Penalties: “Bad Actor” Bans

- SEC proposed rule in June 2011 to implement Sec. 926 of Dodd-Frank and prohibit felons and “bad actors” from Regulation D offerings
- Disqualifying Events for “Bad Actors”
 - Criminal convictions regarding certain securities-related matters
 - Court injunctions and restraining orders regarding certain securities-related matters
 - Final orders of certain state and federal regulators (such as state securities, banking and insurance regulators)
 - SEC disciplinary orders
 - Suspension or expulsion from membership in, or suspension or bar from associating with a member of, a securities self-regulatory organization
 - U.S. Postal Service false representation orders



Increased Penalties: Broad Suspensions

- Prior to Dodd-Frank, SEC could only suspend or bar a securities professional within the area where violation occurred
- Section 925 of Dodd-Frank provides that a bar or suspension of a securities professional is extended to association with other securities firms in other areas



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Part II: The Impact of Title IX on Civil Litigation

*Power to the Plaintiffs!
(including the SEC...)*



Control Person Liability

- Eliminates SEC's prior reluctance to attempt to use this as a cause of action
- Circuit split remains regarding standard of conduct
 - Whether control person need be culpable themselves or simply have the power to control the transaction or activity giving rise to liability
 - May give reason for forum shopping by SEC—if it can establish venue—given new nationwide service of process



Control Persons: Protect Yourself!

- § 20(a) Good Faith Safe Harbor
 - No liability where control person acted in good faith and did not directly or indirectly induce the act or acts constituting the violation or causing the action
- Affirmative defense that the control person had in place a reasonable and proper system of supervision and internal control



Aiding and Abetting Violations

- New (lower) standard
 - “Recklessly” provided substantial assistance
 - Liable to the same extent as the person that committed such violation
- (Another) study on possible private right of action



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Part III: Increased Incentives from Whistleblowing



Let's Make a Deal!

- Rules provide for a bounty of 10% to 30% of the aggregate monetary recovery from government enforcement actions for persons who voluntarily provide the SEC with original information about potential violations of the federal securities laws that substantially contributes to a successful enforcement action, resulting in sanctions of \$1 million or more

Effective August 12, 2011



Let's Make a Deal!

- Discretionary limits on the award: Various factors increase or decrease the award percentage
 - Whether the whistleblower used internal compliance processes
 - Whether the whistleblower interfered with internal compliance processes
 - Rules allow for an employee to report information internally while preserving his or her “place in line” for a possible award from the SEC if the employee decides to disclose the same information to the SEC within 120 days of such internal report



Almost Anyone Can Whistle!

- A whistleblower is
 - (Almost) any individual who provides information to the SEC regarding a possible violation of the securities laws that has occurred, is ongoing or that is about to occur
 - May be an employee, agent or someone else outside the company who provides relevant information
 - Also allows anonymous reporting if done through counsel



Well, Not Everyone Can Whistle...

- Rules exclude some individuals from whistleblowing
 - Officers, directors, trustees or partners who are informed of allegations of misconduct
 - Individuals with compliance or audit responsibilities at an entity, who receive information about potential violations
 - Attorneys cannot be whistleblowers on their own behalf in connection with information they obtained in the course of their representation of a client
 - Accountants are ineligible for awards in the context of providing outside auditing services to that company
 - Foreign government officials
 - Individuals with a pre-existing legal obligation to report information about potential violations to the SEC or to other authorities (e.g., government contracting officers)



Exception (Somewhat) Swallows the Rule

- These individuals may report directly to the SEC as whistleblowers to the extent they have a “reasonable basis to believe that disclosure of the information to the Commission is necessary to prevent . . . conduct that is likely to cause substantial injury to the financial interest or property of the entity or investors”
- These individuals may report directly to the SEC 120 days after the individual has reported the information internally to appropriate internal resources



But Only Some Whistles Make the Cut:

- Must provide information to the SEC voluntarily
- Information submitted by individuals pursuant to a pre-existing legal or contractual duty to report violations to the SEC or certain other federal authorities specified in the rules will not be considered “voluntary”



More Conditions for Whistleblowers

- Must provide original—but not necessarily first-hand—information
- Not just any information will do! Information provided must:
 - Be sufficiently specific, credible and timely
 - “Significantly contribute” to the success of an enforcement action concerning conduct already under investigation
 - Be provided to an employer concurrently or before the submission of such information to the SEC and subsequently cause the company to conduct an investigation and disclose information directly to the SEC such that it satisfies one of the first two prongs



Anti-Retaliation Provisions:

Can't stop that whistling!

- Whistleblowers have a private cause of action in the event that they are discharged or discriminated against by their employers for whistleblowing
- Expands application of the protection to all whistleblowers rather than only those whose information leads to a successful enforcement action
- Whistleblower must possess a “reasonable belief” that the information provided relates to a possible securities law violation to be protected



What Should Firms Do About That Whistling?

- Reexamine internal compliance program
 - Are your programs fully communicated to employees and easy to understand and use?
- Tone at the top
 - Employees should be encouraged to report violations through the company's whistleblower hotline
- Reinforce policies against retaliating against whistleblowers