

## **2008 Year in Review: SEC and SRO Selected Enforcement Cases and Developments Regarding Broker-Dealers**

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As it has done over the last several years, the Securities Litigation and Enforcement Practice has published an outline highlighting selected U.S. Securities and Exchange Commission (SEC or the Commission), Financial Industry Regulatory Authority (FINRA), and NYSE Regulation enforcement actions and developments regarding broker-dealers during 2008. This LawFlash provides an executive summary of this year's publication. Read the full outline at [http://morganlewis.com/pubs/2008YearInReview\\_WhitePaper\\_Jan2009.pdf](http://morganlewis.com/pubs/2008YearInReview_WhitePaper_Jan2009.pdf).

Last year was one of dramatic change in the securities industry. The markets were roiled by a number of unprecedented economic events, and the most prominent stock market indices lost significant value, with the Dow Jones Industrial Average declining about 34%, and the Nasdaq closing down approximately 41% from the end of 2007. The year also saw the demise of several broker-dealers, the merger of others, unprecedented federal capital infusions, and a move away from the independent investment banking model toward that of commercial banks. Investors and regulators also witnessed several major scandals, and the media, Congress, and others called for significant modifications to the current regulatory regime.

The year 2008 was also an eventful year at the SEC. Perhaps most importantly, Mary Schapiro, the current FINRA CEO and President Barack Obama's nominee to replace Christopher Cox as the Chairman of the Commission, is awaiting Senate confirmation.

On the enforcement front, in the SEC's fiscal year 2008, the Commission brought 671 enforcement actions, the second-highest number of actions ever, and a slight increase in comparison to the 656 cases initiated in fiscal year 2007. Of note, however, the statistics include more than twice as many cases against public issuers for untimely regulatory filings in fiscal year 2008 versus fiscal year 2007; many of these cases were initiated in the last month of the Commission's fiscal year. Moreover, in one of its core areas—the regulation of broker-dealers—its caseload was down significantly from about 89 cases in fiscal year 2007 to about 60 cases in fiscal year 2008, a decline of approximately 33%.

The SEC's civil penalties and disgorgement were also significantly lower than in prior years. In fiscal year 2008, the SEC obtained orders imposing \$256 million in civil money penalties, which represents approximately half the amount in fiscal year 2007. The Commission also obtained orders requiring securities law violators to disgorge approximately \$774 million, which is a 29% decline from fiscal year 2007. One of the few statistical bright spots for the SEC occurred in its efforts to close cases. In fiscal

year 2008, the Division of Enforcement closed 1,355 cases, a 260% increase from the prior year.

In 2008, the SEC brought actions relating to auction rate securities, insider trading, online account intrusion, Regulation S-P, market manipulation, stock loan, and conflicts of interest. The Commission also spent time, effort, and resources litigating several market-timing and late-trading cases that it had initiated in prior years. Moreover, the SEC launched intensive examinations and investigations concerning new topics, such as the malicious creation and spread of rumors intended to manipulate securities prices and the alleged Ponzi scheme attributed to Bernard Madoff. In 2008, the Division of Enforcement found itself the subject of several investigations conducted by the Commission's Office of the Inspector General concerning its handling of certain inquiries. The Division of Enforcement also published its Enforcement Manual, which describes its key investigative practices. A discussion of SEC enforcement statistics, priorities, actions, and enforcement developments in 2008 can be found on pages 4-58 of the outline.

One of the most important enforcement efforts in 2008 involved the auction rate securities market; state regulators played an active role in these matters. Accordingly, while in the past this outline has focused entirely on SEC and SRO enforcement, this year we include a section devoted entirely to enforcement matters involving auction rate securities at the SEC, SRO, and state levels, which appears on pages 59-83 of the outline.

Last year was the first full year since the merger of NASD Regulation and NYSE Regulation and the resulting creation of FINRA in late July 2007. FINRA has confirmed that in calendar year 2008, 946 new cases were initiated, 14 member firms were expelled, 321 individuals were barred from membership, and 300 individuals were suspended. In addition, a total of \$1.2 billion in restitution or reimbursement was agreed to in various settlements executed in 2008. That figure includes the agreements in principle relating to the contemplated "buybacks" of auction rate securities discussed on pages 59-83 of the outline. Based upon our review, however, it appears that the number of FINRA enforcement cases with large fines is lower than the number of such cases brought in the recent past by NASD and NYSE Regulation. Indeed, it appears that there were two FINRA settlements in which the fine imposed was greater than \$1 million and one Hearing Panel Decision in which the fine imposed was \$1.53 million.

In 2008, FINRA brought enforcement actions on various traditional topics, including variable annuities, mutual fund sales practices, markups, municipal securities, and form filings. In addition, a sweep action relating to trade volume reporting and a multi-firm OATS case were announced this year. FINRA also brought significant cases in the insider trading and continuing education training areas. As to its regulation and enforcement program, FINRA reported that it completed the creation of a single examination program and enforcement arm; work concerning the consolidation of its rulebook occurred in 2008 and will continue in the coming year. FINRA also published important guidance concerning its views on member firm cooperation. A discussion of FINRA's enforcement statistics, priorities, actions, and new developments in 2008 can be found on pages 84-123 of the outline.

Notwithstanding its merger with the NASD, NYSE Regulation retained oversight and enforcement responsibility for trading violations occurring on the NYSE's systems and facilities. NYSE Regulation announced enforcement actions in 2008 against broker-dealers and individuals—albeit at substantially reduced levels—on a variety of topics, including order marking, supervision of post-execution changes, odd lot trading, and Rule 92. A discussion of NYSE Regulation's enforcement actions in 2008 can be found on pages 124-134 of the outline.

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