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HANDLING A REGULATORY INVESTIGATION II

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HANDLING A REGULATORY INVESTIGATION II – OUTLINE

I. Introduction – Panelists and Overview

II. Getting Started – Representation, Privilege, and Other Preliminary Issues

A. Learn the Facts

1. Upon learning of an investigation by the Securities and Exchange Commission, ("SEC" or "Commission"), company counsel should promptly take steps to learn the facts and begin the process of determining the extent of the company's potential exposure.

2. This process will help inform counsel's initial decisions regarding who it can represent, whether to conduct an investigation, whether to waive privilege in connection with any investigation it conducts, and how generally to comport itself in the investigation.

3. At this early stage, firm counsel may learn sufficient facts to recommend remedial action such as the suspension or termination of culpable employees, a change in firm policies and practices and/or remediation of investor harm. This may be of assistance to the firm at the end of the investigation.

B. Who Does Counsel Represent?

1. Firm counsel must determine what officers/employees it can represent and what employees should have separate counsel.

2. Some cases are clear – where an employee appears to have acted in violation of the law and firm policy, that employee should have separate counsel. The firm may or may not pay for that counsel, depending on the circumstances.

3. Cases that are less clear can include circumstances where the employee may provide evidence against the firm, whether or not that employee has individual exposure.

   a. Former employees can be represented by firm counsel, though they often request separate counsel. Firms differ on whether and when they will pay for separate counsel for former employees. The government can no longer pressure a firm to refuse to pay for counsel for individuals. *See United States v. Stein*, 495 F. Supp. 2d 390 (S.D.N.Y. 2007).

4. The need for separate counsel may be trickier and more pronounced where clients have potentially competing interests in cooperating with regulators (*see* Section II C, below) and where there are parallel actions and/or investigations (see Section VI, below).

a. While clients typically may consent to representation notwithstanding a conflict, some conflicts may be deemed to be "nonconsentable." *See, e.g.* New York Rules of Professional Conduct Rule 1.7 comments 14-17.

b. *See also United States v. Nicholas,* 600 F. Supp.2d 1109 (C.D. Cal. 2009), *rev'd, U.S. v. Ruehle,* 583 F.3d 600 (9th Cir. 2009). In *Nicholas*, outside counsel represented Broadcom in an internal investigation of its stock option granting practices, while at the same time representing the company's CFO in two shareholder suits arising out of those practices. In the course of its internal investigation, counsel interviewed the CFO, but did not inform him that they were representing only the company at that meeting, not him individually or that whatever he said to them could be used against him by the company or disclosed to third parties. The company thereafter disclosed to outside auditors, the SEC and the U.S. Attorney's Office the statements made by the CFO in the investigative interview. A criminal action was commenced against him, and he sought to suppress those statements on the ground that they were privileged. The district court agreed, holding that the CFO reasonably believed that outside counsel met with him as his personal lawyer, not just as company lawyers. The *Upjohn* warning that outside counsel claimed to have given was "woefully inadequate under the circumstances", if in fact it was even given and, in any event, as a warning given to non-clients, was insufficient to terminate an existing attorney-client relationship or obtain an informed waiver of privilege. In addition, the court found that outside counsel breached its duty of loyalty to the CFO by (1) failing to disclose and obtain his informed consent to the clear existence of a conflict (since the company might contend that the CFO was responsible for any wrongdoing in connection with stock option practices) (2) interrogating him for the benefit of the company without his "free and intelligent consent, given with full knowledge of all the facts and circumstances; and (3) disclosing his privileged communications to third parties without consent. On appeal, the Ninth Circuit reversed the suppression order, finding that the CFO did not have a reasonable expectation of confidentiality when he made the statements at issue because he was aware that counsel would share them with the company's auditors. Whether the lawyers had committed ethical violations was not before the appellate court.

C. <u>Determining Strategy – Gather Facts? Conduct Investigation? Cooperate?</u>

1. The strategy you choose is likely driven by the facts you learn, the degree of culpability you have, and the party you represent.

2. When to conduct an "investigation," as opposed to merely gathering facts in preparation for the defense of a case, is an important strategic decision.

a. If an investigation is to be conducted, one must decide whether it can be done internally or by firm counsel, or whether independent counsel should be retained. If fraud is suspected or senior management is involved, independent counsel is advisable.

b. The regulator will expect to learn the results of any investigation. *See* Section II D, below.

3. Firms must live with their regulators for the long term. Some degree of cooperation is necessary to maintain a reasonable working relationship. A series of new initiatives to foster cooperation, begun in 2009, underscores the importance regulators place on cooperation.

a. In March 2010 the Commission announced a number of incentives for individuals and companies to cooperate and assist in SEC investigations and enforcement actions. The staff of the Division of Enforcement now has available to it "cooperation tools" to encourage individuals and companies to report violations and provide assistance. The tools are similar to those used regularly by the Justice Department in criminal investigations and prosecutions, and include cooperation agreements, deferred prosecution agreements and non-prosecution agreements. *See* Enforcement Manual, Securities and Exchange Commission Division of Enforcement, § 6 ("Enforcement Manual").

b. The Commission also set out, for the first time, the analytical framework it uses to evaluate and credit cooperation by individuals. S*ee* Policy Statement Concerning Cooperation by Individuals in its Investigations and Related Enforcement Actions, 17 CFR § 202.12 (Jan. 13, 2010).

c. The so-called "Seaboard Report" details the factors the Commission considers when evaluating cooperation by companies. *See* Commission Statement on the Relationship Cooperation to Agency Enforcement Decisions, SEC Rel. No. 44, 969 (Oct. 23, 2001).

4. Enhanced incentives to cooperate present heightened ethical concerns for counsel representing multiple clients. It may be in the interest of each to be the first to offer cooperation, but only one can be the first to come forward. Or, one client may be well-served by providing evidence that is not helpful to another.

a. The Staff has made clear that it will evaluate and raise ethical issues with counsel in the context of multiple representations, if it appears that a conflict of interest exists.

D. Privilege Issues

1. If you conduct an internal investigation, you should treat it as privileged and confidential unless and until you affirmatively decide to waive the privilege.

2. For a time, criminal authorities and regulators required waiver of the attorney client privilege in connection with internal investigations in order to receive "credit" for cooperation. This is no longer the case. *See* "Principles of Federal Prosecution of Business Organizations," Memorandum from Mark R. Filip, Deputy Attorney General, to Heads of Department Components and United States Attorneys (Aug. 28, 2008). *See also* Enforcement Manual § 4.3 at 99 ("The staff should not ask a party to waive the attorney client privilege or work product protection without prior approval of the Director or Deputy Director.").

3. The assertion of a legitimate claim of attorney-client privilege or work product protection will not negatively affect a claim to credit for cooperation. "The appropriate inquiry in this regard is whether, notwithstanding a legitimate claim of attorney-client privilege or work product protection, the party has disclosed all relevant underlying facts within its knowledge." Enforcement Manual § 4.3 at 101. Consider alternatives:

   a. For example, corporate counsel need not produce, and the staff may not request without approval, protected notes or memoranda generated by counsel's witness interviews. But to receive credit for cooperation, the corporation must produce "and the staff always may request, relevant factual information – including relevant factual information acquired through those interviews. *Id.* at 100.

4. Factors to consider when deciding whether to waive privilege are whether class action or private civil litigation has been or is likely to be instituted, whether the waiver is likely to shorten the investigation done by the government, and whether a waiver will enable the negotiation of a better resolution of the regulatory investigation.

5. If firm counsel interviews employees in connection with a regulatory inquiry, whether or not it is part of an investigation, counsel should advise the employees that, although the interview is a privileged and confidential communication, the privilege belongs to the firm and not the employee, and it can be waived by the firm even if the waiver is not in the employee's best interest.

E. Other Preliminary Issues

1. Document Preservation

   a. At the first hint that the SEC is initiating an investigation, steps should be taken to ensure that all relevant documents, including electronic records, are maintained.

   b. Public companies and firms often issue what is commonly called a litigation hold – generally a memorandum directing the suspension of destruction of documents. The extent of the litigation hold varies, depending on the circumstances. It can require certain people to retain

all documents or can require a broader group of people to retain documents pertaining to particular issues. These litigation holds include emails.

c. Rule 17a-3 describes the records that must be created and maintained by broker-dealers, and Rule 17a-4 addresses record retention periods and accessibility requirements. In particular, Rule 17a-4 provides, in pertinent part, "[e]very [] broker and dealer shall preserve for a period of not less than 3 years, the first two years in an accessible place . . . [o]riginals of all communications received and copies of all communications sent by such member, broker or dealer (including inter-office memoranda and communications) relating to his business as such." 17 C.F.R. § 240.17a-4(b) and (4).

d. In some instances, it may be appropriate to include in the litigation hold the preservation of documents maintained separately from the client's systems.

e. Even if the SEC has not yet requested production, destruction of documents can expose a person to criminal prosecution for obstruction of justice. *See United States v. Fineman*, 434 F. Supp. 197 (E.D. Pa. 1977) (finding that a defendant's knowledge that a grand jury investigation had begun at the time he intentionally destroyed documents was sufficient basis to convict on an obstruction of justice charge); *see also* Press Release 2004-9, "SEC Brings Enforcement Against Bank of America Securities for Repeated Document Production failures During a Pending Investigation, SEC News Release 2004-29 (Mar. 10, 2004); Sarbanes-Oxley Act § 802,18 U.S.C. § 1519 (imposing fines and/or imprisonment of any person who "knowingly alters, destroys, mutilates, conceals, covers up, falsifies, or makes a false entry in any record, document, or tangible object with the intent to impede, obstruct, or influence" an investigation by U.S. department or agency).

f. Additionally, destruction of documents can make substantially more difficult the defense both of the SEC investigation and of any private litigation. *See Coleman (Parent) Holdings, Inc. v. Morgan Stanley & Co., Inc.* No. CA 03-5045 AI, 2005 WL 679071 (Fla. Cir. Ct. Mar. 1, 2005) (jury added $850 million in punitive damages to its verdict upon a finding that Morgan Stanley had not engaged in the electronic discovery process in good faith.).

F. Firm as Public Company – Disclosing Existence of an SEC Investigation

1. Federal securities laws do not specifically require that firms that are publicly traded disclose when they are the subject of an investigation.

2. However, disclosure may be required if the existence of the investigation is material within the meaning of the federal securities law. *See* Regulation S-K.

(17 C.F.R. Part 229). *See also See United States v. Matthews*, 787 F.2d 38 (2d Cir. 1986); *United States v. Crop Growers Corp.*, 954 F. Supp. 335 (D.D.C. 1997). Counsel should also consider whether current circumstances require that existing disclosures be modified or withdrawn.

3. Firms may be involved in many investigations involving trading and supervision that are not "material" in the sense that disclosure is required. On the other hand, recent investigations on auction rate and subprime issues likely require disclosure.

4. Generally, the SEC does not disclose the commencement of an enforcement probe.

   a. Recently, the SEC has disclosed "sweeps" in an effort to show it is taking action during the financial crisis.

G. Notifying Employees

1. It is prudent to notify company personnel that they might be contacted by the staff of the SEC Division of Enforcement ("Staff") and remind them of their rights and responsibilities.

2. The company should also remind the employee to contact the company promptly after being contacted by a law enforcement official.

3. An assertion of the Fifth Amendment by a registered person usually leads to the termination of employment by the firm. Financial Industry Regulatory Authority ("FINRA") Rule 8210 gives FINRA staff the right to require persons associated with member firms to supply information in connection with a FINRA examination. The FINRA's regulations are subject to review and approval by the SEC, and its decisions are subject to SEC review, but courts have held consistently that it is a private body and therefore the Fifth Amendment privilege against self-incrimination does not apply to its proceedings *(see, e.g. D.L. Cromwell Investments, Inc. v. NASD Regulation, Inc*., 132 F.Supp.2d 248 (S.D.N.Y. 2001), *aff'd*, 279 F.3d 155 (2d Cir. 2002)).

III. Document Collection, "Voluntary" Interviews, and Testimony

A. Retention of Documents:

1. Once a firm becomes aware of an investigation, even if it has not yet received a subpoena or request for documents, it is advisable for the firm and counsel to identify relevant individuals and sets of documents or materials that are likely to be most relevant to the case

2. Counsel should prepare and send out a memorandum detailing document retention procedures with respect to relevant materials.

3. Particular concerns arise in regards to electronic information and email systems. The Information Technology (IT) Department must be involved in this process. Normal retention protocol must be identified and possibly adjusted. This can be expensive for the company. *See* Rule 17a-3 for specific rules relating to broker-dealers.

4. Thoroughness is of paramount importance. The SEC often asks witnesses whether documents that were responsive to subpoenas existed but have been destroyed. In connection with its settlements, the SEC now requires a sworn representation that diligent inquiry has been made of sources reasonably likely to have responsive documents and that those documents have been produced or identified in a privilege log. *See* Enforcement Manual § 3.2.6.2.6 at 68.

B. Document Requests

1. As part of itsinitial assessment, the SEC may seek the voluntary production of documents. Usually, the Staff sends a letter, but such a request often is transmitted via the telephone or email, as opposed to subpoena.

2. The firm should treat requests for the voluntary production of documents as though they are subpoenas.

3. The same degree of diligence is required. Always confirm in writing what you understand that you have been asked to provide and what you have in fact provided.

C. "Voluntary" Interviews

1. The Staff may also wish to informally interview relevant employees on a voluntary basis. While employees are not "required" to appear under these circumstances, a refusal to appear voluntarily is seen as a reason to seek a Formal Order, and such refusal will generally be followed by a subpoena requiring an appearance and testimony.

2. Voluntary interviews may or may not be transcribed. Voluntary testimony is transcribed. Counsel may wish to discuss with the Staff their preferences. If the appearance is not transcribed, there is no formal record, and it is likely that the person being interviewed is solely a witness and not a person of interest to the Staff. However, the Staff may call the person for "on the record" testimony at a later date.

3. It is generally preferable to keep the investigation informal because it may provide counsel and the firm with greater control over the scope and timing of document requests and testimony.

4. The witness can be prosecuted for providing false information to a federal official, regardless of whether the interview is formal or informal, transcribed or not transcribed, and under oath or not under oath.

D. Formal Orders

1. In 2009, the Commission approved an order that delegates to the Director of the Enforcement Division the authority to issue formal orders of investigation and the accompanying subpoena power. The Director, in turn, delegated that authority to senior officers throughout the Division. This means that if enforcement Staff encounters difficulty in obtaining documents or testimony or needs to seek information from third parties, or if it decides that the investigation is of some importance, it need only obtain senior supervisor approval.

2. The Formal Order "launches the formal investigation, defines its scope, and establishes limits within which investigative staff may resort to process." *SEC v. Jerry T. O'Brien, Inc.*, 704 F.2d 1065, 1066, n.1 (9th Cir. 1983).

3. Advance notice of the decision to seek a Formal Order is often not provided to the company or counsel – leaving counsel with little opportunity to argue against its issuance. *See SEC v. Arthur Young & Co.* 584 F.2d 1018 (D.C. Cir. 1978).

4. In fiscal 2009, the SEC issued 496 Formal Orders – an increase of more than 100% over the prior year.[1]

E. Subpoenas Generally

1. Once a Formal Order has been issued, any of the designated Staff members may issue subpoenas calling for the production of documents and/or testimony, without any further authorization.

2. Rule 8 of the Commission's Rules Relating to Investigations describes process for serving subpoenas. In practice, subpoenas are often simply mailed or emailed to counsel.

3. Subpoena power reaches anyone in the United States and can require the appearance of witnesses anywhere in the United States. *See* Exchange Act § 21(b), 15 U.S.C.S. § 78u(b). In practice, the timing and location of a witness's appearance is the subject of negotiation with the Staff.

4. SEC subpoenas are not self-enforcing. The SEC must file an action in the appropriate United States District Court to compel compliance.

5. There is little ability to successfully challenge subpoenas. Challenges typically fall into four categories: (1) the investigation is outside the authority of the SEC, (2) the SEC lacks reasonable cause to conduct investigation, (3) the investigation is being conducted in bad faith or for an improper purpose, and (4) the subpoenas are overbroad or unduly burdensome. Such challenges are almost never successful.

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[1] The SEC's fiscal year begins on October 1.

F. Subpoenas for Documents

1. Generally, a firm must produce all responsive non-privileged documents unless the Staff has agreed that certain responsive documents need not be produced.

2. Document subpoenas are increasingly likely to be extremely broad. Often the Staff does not appreciate the breath and burdensomeness of what they have subpoenaed. A firm can often negotiate the scope and timing of its production.

    a. Production of emails presents a particular problem. The Staff is increasingly willing to negotiate an email production based on a search for an agreed upon list of key words.

3. Increasingly, the SEC requests production in an electronic format. SEC subpoenas provide specific requirements for electronic production. Consulting firms are often retained to assist in the document production process. Consulting firms require close supervision, and counsel should maintain control over decisions and process.

4. The consequences for failure to produce documents timely and completely can be severe.

    a. In May 2006, the SEC sued Morgan Stanley & Co. for allegedly failing to produce emails and electronic records in a timely manner during the course of two separate SEC investigations. To settle the action, Morgan Stanley, among other things, agreed to pay a $15 million fine, $5 million of which was to be distributed to the NASD and the NYSE in separate related proceedings. Morgan Stanley also agreed to implement email document preservation and production policies, procedures, and training, and to hire an independent consultant to review the company's reforms.

5. In May 2004, Lucent agreed to pay a $25 million penalty for its lack of cooperation in an SEC investigation. In part, Lucent's penalty for its failure to cooperate was based on it providing incomplete document production, producing key documents after the testimony of relevant witnesses, and failing to ensure that a relevant document was preserved and produced pursuant to a subpoena.

G. Subpoenas for Testimony

1. Testimony is taken under oath, and a witness is subject to penalties for failing to testify truthfully. It is imperative to test your witness to be comfortable he or she is not committing perjury.

a. The consequences for lying in SEC testimony are severe. Peter Baconovic, Martha Stewart's broker, was sentenced to 5 months in prison in 2004 for lying about a suspicious stock sale to the SEC during a deposition.

b. In 2004, Eric I. Tsao, a former executive at MedImmune, Inc., pled guilty to one felony count of criminal insider trading and one felony count of perjury arising from false statements that Tsao made to the SEC Staff during the insider trading investigation. Tsao was sentenced to 15 months for the perjury and the improper the insider trading.

c. Counsel must consider whether to invoke the Fifth Amendment. *See* Section 6 below on Parallel Proceedings. Again, an assertion of the Fifth Amendment by a registered person will in all likelihood result in his or her termination by the firm.

2. Counsel is not technically allowed to object to SEC questions, but in practice, attorneys often note for the record defects in questions or ask that questions be restated for clarity. There is no benefit to counsel being difficult or confrontational. Angering the Staff exposes the client to greater harm.

3. Counsel can usually purchase a transcript of a client's testimony.

IV. Communicating with the Regulator

A. Throughout the investigation, company counsel should attempt to maintain communications with the Staff regarding both procedural matters and the substance of the investigation:

1. Such communications reduce the risk of any misunderstandings that could prolong the investigation and increase the chance of counsel identifying an early opportunity for favorable resolution of the inquiry.

B. During the investigative stage, it is best to deal with the Staff attorney and the branch chief unless their position is untenable.

1. If you feel an appeal to a higher authority is necessary, it is generally advisable to tell the Staff lawyer that you would like to consult with his supervisors.

C. Memorialize Important Communications

1. All important conversations with the Staff, such as conversations where the Staff agrees to a limitation on what documents need to be produced, should be memorialized in a letter to the Staff member.

V. The Wells and Wells-Like Process

A. Definition of Wells Notice

1. A communication from the Staff in which the Staff advises that it intends to recommend to the Commission that it institute enforcement proceedings against the recipient.

2. Rule 5(c) of the SEC's Rules on Informal and Other Procedures outlines authority for a Wells Notice.

B. Details about Wells Notices

1. The Staff must obtain the approval of an Associate Director or Regional Director before issuing a Wells Notice. *See* Enforcement Manual § 2.4 at 28. The SEC Enforcement Manual outlines what the Staff should consider before issuing a Wells Notice. *See id.*

2. The Wells Notice informs the individual or entity of the specific charges the Staff is considering recommending to the Commission and accords the recipient the opportunity to make a submission addressing the reasons why the Commission should not bring an action against them or bringing any facts to the Commission's attention in connection with its consideration of the matter. *See* Enforcement Manual § 2.4 at 29.

   a. Recipients of a Wells Notice may request access to the record and the Staff may, in its discretion, allow recipients to "review portions of the investigative file that are not privileged." In evaluating a request for access, the Staff will consider whether access would be a productive way for both sides to assess the strength of the evidence that forms the basis of the Staff's charging recommendation, whether the requesting party "failed to cooperate, invoked his Fifth Amendment rights, or otherwise refused to testify during the investigation," and the stage of the investigation, including whether other witnesses have yet to testify. Enforcement Manual § 2.4 at 30.

   b. The Staff will generally meet with counsel to discuss in greater detail the evidence on which it is relying and the reasons for its concern.

3. Do you always provide a submission? If not, when?

   a. Wells submissions are expensive. Sometimes it is best to negotiate a resolution of the matter without making a Wells submission. On the other hand, if the Staff's settlement demands are unreasonable, a Wells submission may inform both the Staff and the Commission of the weaknesses in their case.

b. It is virtually impossible to make a credible Wells submission if you have asserted your Fifth Amendment rights and refused to testify. One cannot contest the facts asserted by the Staff without risking a waiver of the privilege.

c. The content of a Wells submission is usually admissible under Federal Rule of Evidence 408.

d. A Wells submission is not privileged or confidential and is discoverable.

VI. Parallel Investigations

A. Generally

1. Parallel investigations are simultaneous adjudicative proceedings that arise out of a single set of transactions and directed at the same individuals. Most often, this involves the SEC and the U.S. Attorney's Office but can include state agencies self regulatory organizations and, increasingly, Congressional commissions and committees. Often, an individual's freedom is on the line in the criminal case while his or her pocketbook and reputation are on the line in the civil investigation.

a. In fiscal 2009, the SEC filed 154 actions in coordination with criminal actions (indictments, informations or contempt proceedings) brought by the Department of Justice. This is an increase of more than 30% over fiscal 2008.

b. In the current regulatory and political climate, there are a number of newly created or newly invigorated governmental actors using the same or similar statutory authority and tools to conduct sometimes overlapping inquiries. For example,

(i) In 2009, Congress established a Financial Crisis Inquiry Commission ("FCIC") to conduct a comprehensive investigation of 22 specific and substantive areas related to the financial crisis. The FCIC is empowered to hold public hearings, issue subpoenas and make criminal referrals to federal and state authorities. With its report to Congress and the President due at the end of 2010, the first FCIC hearings began in January. The FCIC is conducting its own review of accounting practices employed by Lehman Brothers (along side federal prosecutors and others) and will expand that review to examine how pervasive those practices are on Wall Street.

(ii) The previously established Permanent Subcommittee on Investigations ("PSI") and the Public Company Accounting Oversight Board ("PCAOB", along with newly created organizations such as the Office of the Special Investor General

for the Troubled Asset Relief Program ("SIGTARP") all have some overlapping investigative authority.

2. Such parallel proceedings are generally constitutional – as long as the government did not bring the civil action "solely to obtain evidence for the criminal prosecution." *See United States v. Kordel*, 397 U.S. 1 (1970*); SEC v. Dresser*, 628 F.2d 1368 (D.C. Cir., *en banc*) (1980), *cert. denied*, 449 U.S. 993 (1980).

3. SEC Enforcement Staff have recognized that overlapping investigations present significant challenges to all and pledged to work efficiently with other agencies to relieve unnecessary burdens. In the area of cross-agency cooperation, whereas the Staff previously could grant federal and state agency unrestricted access to its regulatory file, including witness proffer statements, the Commission's standard proffer agreement has been revised to provide that any agency seeking access to the Staff's files can obtain copies of witness proffers only if that agency agrees to abide by the same terms and conditions as the Commission.[2]

4. A challenge to parallel proceedings based on double jeopardy generally will fail. *See Hudson v. United States,* 522 U.S. 93 (1997).

   a. All SEC settlements contain "boilerplate" language making the settling party waive any claim of double jeopardy.

B. Fifth Amendment:

1. Parallel investigations often pose a Fifth Amendment dilemma. Statements made in civil discovery or investigations can be used against an individual in criminal proceedings while remaining silent can result in an adverse inference in a civil proceeding.

C. *United States v. Stringer*, 408 F. Supp.2d 1083 (D. Or. 2006).

1. The District Court found that the SEC had made a conscious effort to conceal the criminal investigation which constituted "deceit, trickery, or intentional misrepresentation." The Ninth Circuit reversed, finding that the witness had sufficient notice of the possibility of parallel proceedings. The decision highlights the difficult choices faced by companies and individuals in dealing with such parallel investigations.

2. If you do not know whether there is an interest in the matter by criminal authorities, you should either ask or assume that any documents you supply or testimony you give will be shared with criminal authorities.

D. Factors in Asserting Fifth Amendment

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[2] *See* The SEC Speaks 2010: Fast-Paced Reform Continues in 2010, Morgan Lewis Securities Lawflash (February 11, 2010), http://www.morganlewis.com/pubs/SecuritiesLF_SECSpeaks2010_11feb10.pdf.

1. If there is criminal interest, what factors should you consider in deciding whether to assert your Fifth Amendment rights?

   a. Did your client engage in criminal wrongdoing?

   b. If your client testifies, will you improve his or her chances of avoiding criminal prosecution?

   c. How good will your client be as a witness? and

   d. Can you get immunity for your witness?

E. Collateral Estoppel

1. A criminal conviction operates as an estoppel in a subsequent civil proceeding.

F. Potential Strategies for Defense Counsel

1. Seek a stay of the civil proceeding.

2. Seek a protective order as to certain evidence.

3. Seek immunity from criminal agencies.

4. Seek a global settlement.

VII. How Does it End? – Concluding the Investigation

A. Inquiring Whether the Case is Ongoing

1. Whether to ask such a question poses a dilemma for defense counsel, but the new Enforcement Manual states that "the staff is encouraged to close an investigation as soon as it becomes apparent that no enforcement action will be recommended." Enforcement Manual § 2.6.1 at 38. It is "the Division's policy . . . to notify individuals and entities at the earliest opportunity when the staff has determined not to recommend an enforcement action against them to the Commission. Enforcement Manual § 2.6.2 at 40.

2. The Staff is permitted to send termination letters before the investigation is closed.

B. Settlement

1. Many cases are settled before an enforcement action is brought, but settlements can and do also occur after an action has been brought.

a. Defense counsel can initiate settlement discussions at any time. This is a strategic decision driven by counsel's perception as to whether an enforcement action is inevitable and how strong the case against his or her client is.

b. If an action is inevitable and the SEC's case is strong, then an attempt to settle at an early stage may be advisable. The desirability of an early settlement may be influenced by whether there is a parallel criminal investigation or pending civil litigation.

2. Settlements with the SEC are "without admitting or denying" wrongdoing or liability. This may be preferable to litigating and risking findings of liability.

a. The SEC does not permit defendants or respondents to deny liability after a settlement. After an agreement in principle was reached between the Lucent and the SEC staff, Lucent's counsel characterized Lucent's actions as a "failure of communication," thus suggesting that an accounting fraud had not occurred. According to the SEC, Lucent's public statements undermined both the spirit and letter of its agreement in principle with the staff. The denial of liability formed part of the basis for the $25 million penalty imposed on Lucent in May 2004.

3. The language of the SEC's complaint cannot be "negotiated," but it can be influenced in the context of a settled proceeding.

C. Initiate Action

1. The SEC files civil complaints in federal court or administrative proceedings before "captive" administrative law judges.

a. These proceedings are accompanied by a press release.

2. The SEC seeks the following types of relief:

a. Court-ordered injunction barring the defendant from future violations.

b. A cease-and-desist order ordering the respondent to cease and desist from future violations.

c. An order suspending or barring an individual from associating with a broker dealer or investment advisor.

d. An order compelling disgorgement of any unjust enrichment.

e. An order imposing penalties.

f. An order barring an accountant or attorney or other professional from practicing before the Commission.

g. If the action involves financial statements or disclosures by a firm, which is also a public company, the relief sought can include an order requiring a company to restate its financial statements or otherwise correct material misstatements, and an order barring an individual from serving as an officer or director of a public company.

h. An order imposing other remedial relief.