

## Enhancements of SEC Enforcement Authority by Dodd-Frank

The historic and sweeping Dodd-Frank Wall Street Reform and Consumer Protection Act (Act or Dodd-Frank) recently signed into law by President Obama contains several significant enhancements to the enforcement authority and jurisdiction of the SEC. Some of these enhancements are explained in further detail below.

### *Aiding and Abetting Liability*

The Act amends the Securities Act of 1933 (Securities Act) and the Investment Company Act of 1940 (Investment Company Act) to provide the SEC with authority to prosecute persons who aid and abet violations of those acts. Previously, the SEC only had authority to prosecute aiders and abettors who “knowingly” substantially assisted violations of the Securities and Exchange Act of 1934 (Exchange Act) or who had aided and abetted violations of the Investment Advisers Act of 1940 (Advisers Act). Additionally, under Dodd-Frank, the SEC may pursue “reckless” aiders and abettors as well as “knowing” ones. The Act does not extend aiding and abetting liability to private actions, but commissions the Government Accountability Office to study the impact of such an extension. The Act also clarifies the SEC’s ability to pursue enforcement actions against “control persons” under the securities laws.

### *Civil Penalties in Cease-and-Desist Proceedings*

The Act amends the Securities Act, Exchange Act, Advisers Act, and Investment Company Act to grant the SEC the authority to impose monetary penalties in all of its cease-and-desist proceedings. Previously, the SEC only had the authority to impose monetary penalties in cease-and-desist proceedings against registered entities and persons associated with registered entities.

### *Collateral Bars*

Dodd-Frank grants the SEC the authority to impose securities-industry-wide suspensions or bars so that, for example, the SEC may now suspend or bar a person who commits a securities violation while associated with a broker-dealer not only from associating with a broker-dealer, but also with an investment adviser, municipal securities dealer, or other such regulated entity. Previously, such suspensions or bars could only be imposed with regard to the capacity in which the person had committed the violation.

### *Antifraud Provisions*

The Act amends Sections 9, 10, and 15 of the Exchange Act to expand its antifraud provisions. Section 9, which relates to market manipulation, is amended by the Act to cover all securities except government securities, regardless of whether they are registered on a national securities exchange. The reach of Section 10(a), relating to short sale abuses, is similarly extended. Dodd-Frank also extends the reach of Section 9(b) to cover non-exchange transactions in options. Exchange Act Section 9(c) is amended to apply to all broker-dealers, not just members of a national securities exchange, and Section 15(c)(1), which prohibits broker-dealers from engaging in fraud or manipulation in connection with the purchase or sale of an over-the-counter security, is amended to cover exchange transactions as well.

### *Nationwide Service of Trial Subpoenas*

Dodd-Frank provides that in any federal court proceeding instituted by the SEC under the Exchange Act, Securities Act, Advisers Act, or Investment Company Act, both the SEC and defendants may serve subpoenas anywhere in the United States to compel the production of documents or attendance of a witness at a hearing or trial. Federal Rule of Civil Procedure 45(c)(A)(ii), which ordinarily would require a court to quash a subpoena that compelled a person to travel more than 100 miles in order to comply, will not apply to such subpoenas.

### *Proceedings Against Formerly Associated Persons*

The Act amends various provisions of the securities laws to make it clear that the SEC has the authority to bring an action against a person formerly associated with a registered entity, notwithstanding that such person is not currently associated with any registered entity.

## ***Extraterritorial Jurisdiction***

The Act limits the application of the recent Supreme Court decision in *Morrison v. National Australia Bank, Ltd.*, in which the Court held that the anti-fraud provisions in Section 10 of the Exchange Act were not applicable to private actions by foreign investors arising from purchases and sales of securities that occurred outside of the United States. Dodd-Frank provides that federal district courts have jurisdiction over actions commenced by the SEC alleging violations of the securities laws' antifraud provisions "even if the securities transaction occurs outside the United States and involves only foreign investors," if it alleges conduct in the United States that constitutes "significant steps in furtherance of the violation" or conduct outside the United States that has a "foreseeable substantial effect within the United States." The Act also requires the SEC to conduct a study to determine whether the extraterritorial jurisdiction of the federal courts should also be extended to private rights of action under the antifraud provisions.

## ***Deadline for Completing Investigations, Inspections, and Examinations***

In an apparent effort to accelerate the enforcement process, the Act adds a new section to the Exchange Act regarding deadlines for completing enforcement investigations and compliance examinations and inspections. In general, it provides that, not later than 180 days after the SEC staff provides a written Wells notification to any person, the staff must either file an action against the person or provide notice to the Director of the Division of Enforcement of its intent to not file an action. For certain "complex" actions, the staff may be granted one 180-day extension with approval by the Director of the Division of Enforcement and notification to the Chairman of the Commission. After the initial 180-day extension, the staff may be granted additional 180-day extensions in complex actions only with approval of the Commission. Similarly, the SEC's compliance inspections and examinations staff has 180 days from the date it completes an on-site examination or inspection and obtains all requested records to request corrective action or provide notice that the matter is concluded, subject to 180-day extensions on notice to the Chairman of the Commission and subject to Commission approval for successive extensions.

## ***Whistleblower Provisions***

The Act includes significant monetary incentives for individuals with knowledge of securities violations to contact the SEC and provide assistance to the investigation and prosecution of the violations, providing that the SEC "must" pay a bounty of between 10 percent and 30 percent of any monetary sanction of more than \$1 million when information furnished by a whistleblower leads to the enforcement action. The bounty provisions also apply if the information leads to enforcement action by the Justice Department, another federal agency, a self-regulatory organization, or a state attorney general. To qualify for a bounty, the whistleblower must have voluntarily provided information "derived from the independent knowledge or analysis" of the whistleblower that was not known to the SEC from any other source. The Act also provides substantial protections to such whistleblowers.

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