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A New Era of Cooperation at the SEC

The SEC's Division of Enforcement is implementing a series of measures designed to enhance and encourage cooperation in its investigations and litigation and, the Division hopes, expedite the enforcement program. This project is referred to as the "Cooperation Initiative." On January 13, the SEC announced three new tools to be used by the Division, all tools that have been available to, and successfully used by, the Justice Department for many years, including:

1. **Cooperation Factors.** The SEC's enforcement division now can use "cooperation agreements" -- formal written agreements in which the staff agrees to recommend to the SEC that a cooperator receive "credit" for cooperating. The Division, in its enforcement manual, has expressed that it will consider cooperation agreements where the individual has provided or likely will provide substantial assistance but typically will only seek authority for a cooperation agreement after receiving proffers or other information regarding the assistance that can be provided. Even after entering into a cooperation agreement, an individual or company should be aware that the Division's recommendation does not bind the Commission and that only the Commission can make a final determination on an appropriate resolution including settlement parameters.

The SEC issued a policy statement, and updated the enforcement manual, listing standards for evaluating cooperation by individuals. The factors are designed to balance the objective of holding individuals fully accountable for their misconduct against the need to provide incentives for individuals to cooperate. While the SEC has stated that the factors are not all-inclusive, and will vary under the unique circumstances of each case, the four primary considerations are:

- a. The assistance provided by the cooperating individual in an investigation or related enforcement action. This will include an assessment of whether the cooperation was timely and voluntary, helpful, truthful, complete and reliable; and conserved time and resources of the SEC staff.
- b. The importance of the underlying matter in which the individual cooperated. This component will look at, among other things, the character of the investigation including the type and number of potential violations, its subject matter priority, its age and the duration of the conduct, and the amount and type of harm caused by the violations.
- c. The societal interest in holding the individual accountable for his or her misconduct. The SEC will assess the nature of the violations in light of the individual's knowledge, experience and responsibility at the time of the violations; the culpability of the individual generally and in relation to others who participated in the misconduct; the degree to which an individual tolerated or took steps to prevent misconduct; efforts made to remediate the harm such as repaying victims; and sanctions imposed by other authorities or organizations.

- d. The profile of the cooperating individual. A person's profile, for consideration in this component, will include personal and professional factors such as the history of compliance with the law and regulations; an acceptance of responsibility for any misconduct; and the opportunities for future misconduct in the securities field.
2. **Deferred prosecution agreements.** The Division, in appropriate cases, can now recommend that the SEC enter into deferred prosecution agreements, in which the SEC will forego, pending the passage of a specified time, an enforcement action against an individual or entity. The deferred prosecution agreements will contain terms requiring, among other things, full cooperation, a waiver of statutes of limitations, and compliance with certain prohibitions and undertakings during a specified period. Those undertakings could include the payment of disgorgement or penalties. The term of the deferred prosecution agreement should not exceed five years and, unless the SEC directs otherwise, deferred prosecution agreements will be available to the public.
3. **Non-prosecution agreements.** The Division will also recommend, in very limited and appropriate circumstances, that the SEC enter into a non-prosecution agreement with a cooperator. The cooperating individual or company will be required to cooperate fully, testify truthfully, and comply with specific undertakings including, where appropriate, the payment of disgorgement and penalties. In its enforcement manual, the Division notes that non-prosecution agreements should not be entered into in the early stages of investigations and should not be entered into with those who previously violated the securities laws. Non-prosecution agreements likely will be available to the public.

In addition to borrowing these tools from the Department of Justice's practice, the Division of Enforcement announced on January 13, additional measures and made modifications to its enforcement manual designed to facilitate cooperation.

4. **Expedited immunity requests.** In some circumstances, agreements with the SEC may not be enough to obtain the cooperation of a key witness, particularly where they may also be at risk for criminal prosecution. Previously, a request for immunity was required to be made by the Commission directly to the Department of Justice (for either statutory or letter immunity). Now, the Enforcement Director has the authority to submit immunity requests to DOJ. Immunity requests are unlikely in the early stages of an investigation where the role of the witness may be unclear. Moreover, the enforcement manual clarifies that immunity should only be sought where necessary in the public interest.
5. **Early assurances of status and termination notices.** Noted as a "Related Tool" in the cooperation section of the manual, the Division has outlined a process by which an enforcement supervisor may inform an individual or entity that the staff will not be recommending enforcement action against it. While such a statement does not bind the SEC, particularly if new information comes to light, this provision gives the staff much more discretion than it previously possessed. Moreover, the manual states that when an investigation is complete as to a potential cooperating individual or company and the Division has determined, for any reason, not to recommend to the Commissioners an enforcement action against the

individual or company, supervisors may, and in some cases are required, to send a letter informing the individual or company of the determination. If the potential cooperating individual or company is likely to provide substantial assistance and the Division has not entered into a cooperation agreement with the individual or company, these notices may be provided before the Commission's investigation is closed or before a determination has been made as to every other potential defendant or respondent in the case.

In the SEC's announcement, Enforcement Director Robert Khuzami emphasized that the cooperation initiatives are designed to incentivize "extraordinary cooperation," not mere compliance with "routine or ordinary requests." Indeed, the most attractive of these cooperation tools for witnesses, such as immunity or deferred prosecution and non-prosecution agreements, likely will not be available to more than the first and most senior witnesses in the door at the SEC. Significantly, the Enforcement manual states that some of the tools such as the deferred prosecution and non-prosecution agreements, generally will require agreements by an individual to admit the facts of the underlying violations or, at a minimum in other matters, agree not to contest those facts.

For additional information on the SEC's new cooperation initiative, contact one of the attorneys below:

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