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SEC Enforcement Year in Review: Actions and Issues From 2013

By Daniel Marx and Lisa Wood

Not since the Great Depression has so much changed so fast. In 2008 and 2009, the global financial crisis devastated securities markets and the financial services industry. In 2010, Congress responded by enacting the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act).1 Since then, the Securities and Exchange Commission (SEC) has promulgated a vast array of new securities regulations,2 including regulations to enhance the oversight of investment advisers.3 In addition, in 2011 and 2012, the Enforcement Division of the SEC brought new enforcement actions at a record-breaking pace, both in administrative proceedings and also in federal court.[4] Many of these actions targeted investment advisers, from massive firms like The Galleon Group, run by Raj Rajarantam, to much smaller, unregistered advisers.

While recent years have been defined by these new securities laws and the unprecedented levels of enforcement activity, the past year in particular has featured many new faces in the senior leadership at the SEC and its Enforcement Division. Most notably, in April 2013, Mary Jo White became the new Chairman of the SEC, replacing former Chairman Elisse B. Walter.[5] Chairman White brings many years of experience as a federal prosecutor, having served as the US Attorney in Manhattan (from 1993 to 2002) and Brooklyn (on an acting basis, from 1992 to 1993). The nomination of a long-time prosecutor, who spent much of her career prosecuting high-profile criminal cases from international terrorism to insider trading, sends a strong signal to the investment community that aggressive enforcement will remain a central concern, if not the top priority, for the SEC.

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Within the Enforcement Division, Director Robert Khuzami stepped down in January 2013. During his nearly four-year tenure, Khuzami oversaw an historic re-organization of the Enforcement Division, led a Staff that brought thousands of enforcement actions, launched major enforcement initiatives (including the SEC's Cooperation Initiative), and established the Office of the Whistleblower.[6] In April 2013, Co-Directors George Canellos and Andrew Ceresney took the helm at the Enforcement Division.[7] Canellos previously served as the Deputy Director under Khuzami and, before that, as the Director of the New York Regional Office. Ceresney most recently worked as the chief appellate lawyer in the US Attorney's Office in Manhattan, and like Khuzami, both Canellos and Ceresney worked for White as federal prosecutors, serving on the Securities and Commodities Task Force.[8] All three can be expected to draw on their shared law enforcement background with the Justice Department as they lead the SEC and its Enforcement Division.

In May 2013, Chief Bruce Karpati announced his decision to leave the Asset Management Unit of the Enforcement Division, which oversees investigations of investment advisers, investment companies and private funds.[9] Among other initiatives, Karpati contributed to the Aberrational Performance Inquiry, which employs advanced data analysis to uncover suspected fraud by hedge fund managers, as well as the Compliance Program Initiative, which focuses enforcement activity on registered investment advisers who repeatedly fail to implement effective compliance programs. A pioneer in combatting hedge fund fraud, Karpati helped to establish the SEC's Hedge Fund Working Group in 2007. Co-Chiefs Julie Riewe and Marshall Sprung, who served as Deputy Chiefs under Karpati, have stepped into his shoes.[10] Both Riewe and Sprung have been involved in numerous investigations and enforcement actions concerning investment advisers.

Amidst these many personnel changes at the SEC and in the Enforcement Division, the pace of enforcement actions seems to have slowed.[11] Between January 2013 and September 2013, the SEC filed 526 new cases, but approximately 50 percent of them were "follow-on" or "delinquent filer" actions, rather than new matters focusing on the SEC's "core" concerns, such as insider trading.[12] Nevertheless, the SEC made headlines with several high-profile cases in 2013, including its win against Rajat Gupta, the former global head of McKinsey & Co.;[13] its loss at trial against Mark Cuban, the owner of the Dallas Mavericks;[14] and its administrative proceeding against Steven A. Cohen, the owner and manager of SAC Capital Advisors, which has been stayed pending the resolution of related criminal prosecutions against SAC Capital Advisors and two of its former employees.[15] The SEC also settled a major insider trading action against Scott London, a senior audit partner of KPMG LLP,[16] after London pleaded guilty in a related criminal case.

Chairman White has repeatedly stated that, going forward, the SEC intends to litigate more cases through trial to verdict.[17] She has emphasized the benefits, for the SEC and the investment community, of trying cases: public trials bring needed visibility and accountability to the enforcement process, thereby advancing the Enforcement Division's agenda.[18] An experienced litigator, White may be emboldened to have her enforcement attorneys take more cases to trial, because over the past three years, the SEC has won approximately 80 percent of the time.[19]

At the same time, Chairman White has also acknowledged the need for the SEC to pursue settlements in appropriate cases.[20] In the future, however, such settlements may increasingly include admissions of guilt. For example, in August 2013, the SEC reached a global settlement that included admissions of guilt in *SEC v. Philip A. Falcone et al.* and *SEC v. Harbinger Capital Partners, LLC*.[21] Falcone admitted that, among other misdeeds, he improperly borrowed more than $100 million from a fund that Harbinger Capital Partners managed and also granted favorable redemption and liquidity terms to certain large investors.[22] More recently, the SEC settled charges against JPMorgan Chase & Co. alleging that the investment bank had misstated its financial results and lacked proper internal controls.[23] As part of that resolution, JPMorgan admitted certain facts, acknowledged publicly that it had violated federal securities laws and agreed to pay a civil monetary penalty of $200 million.

In summary, over the past year, the SEC has actively pursued enforcement actions that reflect both its traditional agenda and also its current regulatory priorities, such as promoting basic compliance among investment advisers. It has also reckoned with an important decision from the Supreme Court concerning the statute of limitations for enforcement actions, received thousands of complaints and tips from whistleblowers and adopted new enforcement tactics, most notably its first deferred prosecution agreement with a fund administrator who engaged in fraud but then assisted the Enforcement Division with catching bigger fish. Like the dynamic securities markets themselves, the enforcement activities of the SEC have continued to evolve.

I. The SEC's Enforcement Priorities

In addition to actively pursuing its traditional agenda, such as combating insider trading and outright fraud, over the past year, the SEC brought many new cases that clustered around several key rules and represented current priorities for the Enforcement Division concerning investment advisers: Rule 105 of Regulation M, the Compliance Rule, the Custody Rule and valuation issues.

A. Rule 105 of Regulation M

Rule 105 of Regulation M broadly prohibits short selling in advance of secondary offerings. Subject to limited exceptions, a person or entity may not participate in a secondary offering of securities, which is conducted on a firm commitment basis, if that person or entity has sold short the same securities within a five-day restricted period (typically, five business days before the pricing).[24] The aim of this regulation, according to the SEC, is to prevent "manipulative" short selling, which can drive down the prices of securities sold in secondary offerings and undermine the ability of issuers to raise capital.[25]

Since January 2010, violations of Rule 105 have been a major focus of SEC enforcement activity. During this three-year period, the SEC has settled more than 40 actions against firms and individuals (mostly investment advisers), and it has collected more than $42 million in disgorgement, interest and penalties.[26] This program, perhaps more so than any other SEC initiative, reflects the "broken windows" approach to policing the securities markets: by aggressively pursuing violators of Rule 105, the Enforcement Division has tried to "sen[d] a message that [it] will not tolerate any violations—big or small—that threaten the integrity of the capital raising process."[27]

Consistent with this "zero tolerance" approach, on September 17, 2013, the SEC announced charges against 23 firms and one individual for violations of Rule 105.[28] Director Ceresney heralded this "crackdown" by the Enforcement Division, stating that "[t]he benchmark of an effective enforcement program is zero tolerance for any securities law violations, including violations that do not require manipulative intent."[29] Andrew Bowden, who heads the National Examination Program, emphasized the "coordination between the enforcement and examination programs," which "reaffirms that market participants must be in compliance with Rule 105 to preserve and protect the independent pricing mechanisms of the securities market."[30]

This most recent wave of Rule 105 actions ran the gamut from large cases, featuring millions of dollars in disgorgement and civil monetary penalties,[31] to small ones, involving minimal amounts of disgorgement and standard penalties of $65,000 (the Tier 1 maximum penalty per violation).[32] In all, as a result of this recent "crackdown" on Rule 105 violations, the SEC has obtained disgorgement of "ill-gotten" gains from nearly two dozen firms ranging from $4,000 to $2,500,000, "showing that no amount is too small to escape our attention, and that going after smaller infractions will not distract us from larger ones."[33]

While the volume of these Rule 105 actions remains high, and the basic legal issues have stayed the same, the process has changed considerably. Enforcement activity is now centralized in Washington, DC (not spread out among the regional offices), and it is subject to a fairly standard regime. Of the 23 actions brought in September 2013 by the SEC, 22 settled, and the orders in all of those settled cases were based on a common Rule 105 template. According to the SEC, "this new program of streamlined investigations and resolutions of Rule 105 violations ... send[s] the clear message that firms must pay the price for violations while also conserving agency resources."[34] A core element of this program is the uniform formula for disgorgement: typically, a combination of (i) the short profit, which is based upon the difference between the short price and the cover price, and (ii) the offering profit, a measure of the improperly obtained benefit from the offering, which is based upon the difference between the offering price and the volume-weighted average price (VWAP) on the same day. While this formula might be subject to challenge as excessive, arguments to the Enforcement Division Staff have proved unavailing.

All of the investment advisers who have settled Rule 105 actions have taken appropriate remedial steps to implement new policies and procedures. Nevertheless, the SEC has insisted on disgorgement and penalties. The SEC's Risk Alert regarding Rule 105 cautions: "After-the-fact remediation [does] not absolve a firm or individual from the violation of Rule 105."[35] Moreover, because Rule 105 imposes strict liability, once a violation has been established, it is no defense to say that the person or entity who broke the law acted without scienter or fraudulent intent.[36]

Because the legal issues are straightforward and the financial rewards for the SEC are substantial, the enforcement actions concerning violations of Rule 105 will likely continue for the foreseeable future. Thus, advisers must implement effective compliance policies, memorialize those policies in their compliance manuals, train relevant employees concerning those policies, and designate supervisory personnel to ensure compliance with them. Ideally, these steps should be taken before any violation occurs.[37] To minimize the penalties in Rule 105 cases, the SEC also encourages investment advisers to self-report violations of Rule 105 and cooperate with any related investigations.

B. The Compliance Rule

Rule 206(4)-7 under the Investment Advisers Act of 1940 (Advisers Act), also known as the Compliance Rule, requires investment advisers to adopt and implement written policies and procedures that are reasonably designed to prevent violations of securities laws and regulations.[38] The Compliance Rule mandates far more than putting a compliance manual on the shelf, however: "Firms must not only have policies and procedures in place, but also need to properly implement those policies and procedures."[39] For that reason, the Compliance Rule also requires advisers to review their policies and procedures at least once per year to ensure the adequacy and effectiveness of their implementation. It further requires advisers to designate a qualified chief compliance officer (CCO) who is responsible for implementing and administrating the compliance policies and procedures.

In recent years, violations of the Compliance Rule have also been a major focus of SEC enforcement activity, in particular when it comes to repeat offenders and investment advisers who do not promptly and completely remediate deficiencies. From the SEC's perspective, a meaningful commitment to effective compliance begins with the regulatory basics because "minor violations that are overlooked or ignored can feed bigger ones."[40] "Perhaps more importantly," violations of the Compliance Rule "can foster a culture where laws are increasingly treated as toothless guidelines," which undermines the enforcement of securities laws and the integrity of securities markets.[41] For that reason, the SEC's Compliance Program Initiative, a collaboration between the National Examination Program and the Asset Management Unit, "targets firms that have been previously warned by the SEC examiners about compliance deficiencies but failed to effectively act upon those warnings."[42]

Shortly after it launched the Compliance Program Initiative, about two years ago, the SEC brought several enforcement actions involving violations of the Compliance Rule.[43] Continuing these efforts in the past year, the SEC recently announced additional enforcement actions based on similar violations, focusing on firms that failed to remedy compliance deficiencies that the SEC had previously identified.[44] All of these recent actions ended with settlements in which the SEC issued cease-and-desist orders, censured the investment advisers and imposed substantial civil monetary penalties. The advisers also agreed as part of their settlements to retain independent compliance consultants.

In *In the Matter of Equitas Capital Advisors, LLC, Equitas Partners, LLC, David S. Thomas, Jr. and Susan Christina*,[45] the SEC found that Equitas Capital Advisors, LLC (Equitas), a registered investment adviser in New Orleans, Louisiana, which recommends money managers to clients (but does not directly invest their assets), and Equitas Partners, LLC (Equitas Partners), a registered adviser under common control with Equitas, failed to conduct annual compliance reviews and to maintain adequate compliance policies and procedures.[46] Equitas had written policies and procedures, but its compliance manual was modeled on a broker-dealer manual and, therefore, "not sufficiently tailored to Equitas' business of recommending other money managers."[47] The manual failed to address, among other important topics, conflicts of interest that were inherent in Equitas' business model.

These compliance violations occurred "despite warnings" from the Office of Compliance Inspections and Examinations (OCIE).[48] Following examinations in 2005, 2008 and 2011, the OCIE Staff sent deficiency letters to Equitas and Equitas Partners, yet the firms failed to fix their problems. Both David Thomas, the chief executive officer (CEO) of Equitas and Equitas Partners, and Susan Christina, the CCO of the two firms, participated in the examinations by "meeting with the OCIE [S]taff, reviewing the deficiency letters… and preparing and/or reviewing the firms' letter in response."[49] The SEC found that, based upon their personal participation, Thomas and Christina had "aided, abetted and caused" the chronic failures by Equitas and Equitas Partners to implement appropriate compliance policies and procedures and to conduct the required annual reviews.[50]

In addition to these violations of the Compliance Rule, and possibly as a result of them, the SEC also found that Equitas, Equitas Partners and Thomas were not truthful in their disclosures to clients about potential conflicts of interest, fees and examination deficiencies. Specifically, in response to requests for proposals and due diligence questionnaires, Equitas and Equitas Partners negligently provided false and misleading information that omitted any mention of identified deficiencies or, worse, falsely stated that the firms had no such problems.[51] To resolve this administrative enforcement action, Equitas and Equitas Partners agreed to retain an independent compliance consultant for three years and to provide notice of the Order to all of their clients and on their website.[52] The SEC also issued cease-and-desist orders, censured Equitas and Equitas Partners, and levied civil monetary penalties of $100,000 against Equitas and $35,000 against Thomas.

In *In the Matter of Stephen Derby Gisclair*,[53] the SEC pursued a related enforcement action against Stephen Gisclair, a former officer of Equitas and Equitas Partners, who also "aided, abetted and caused" the firms' violations of the Compliance Rule (among other problems).[54] Gisclair had co-founded both firms, and at the relevant times, he served as the CCO of Equitas Partners and the chief operating officer (COO) of Equitas Partners. In these capacities, Gisclair was "the primary liaison" with the OCIE Staff and also the "primary author" of the firms' responses to deficiency letters.[55] The SEC held Gisclair individually responsible for the compliance failures at Equitas and Equitas Partners because he was personally involved with, or responsible for, most of those problems, such as the inadequate compliance manual, misleading statements to investors, and the submission of an inaccurate Form ADV to the SEC. To resolve this action, Gisclair agreed to resign from his position as the CCO of his new advisory firm, Crescent Capital Consulting, LLC, a registered adviser, and to notify all of his clients of the Order against him.[56] The SEC issued a cease-and-desist order against Gisclair and imposed a civil monetary penalty of $90,000.[57]

In *In the Matter of Modern Portfolio Management, Inc., G. Thomas Damasco II and Bryan F. Ohm*,[58] the SEC found that Modern Portfolio Management, Inc. (MPM), a registered investment adviser in Holland, Ohio, and its principals, Thomas Damasco and Bryan Ohm, failed "to correct ongoing violations."[59] After an on-site examination in 2008, the OCIE Staff sent a deficiency letter to MPM, which responded with assurances that it would "take corrective action."[60] MPM failed to follow through on its promise, however. Following another examination in 2011, the OCIE Staff determined that MPM had not completed its annual compliance review in 2009 and that MPM continued to make misleading statements in its marketing materials.[61] Further, the OCIE Staff found that MPM overstated its assets under management, boasting over $600 million on its website but, at the same time, reporting less than $275 million on its Form ADV.[62]

The primary problem at MPM seemed to be that, from the outset, "Damasco and Ohm tasked an employee with less than three months of experience with overseeing compliance at MPM even though that employee had no Advisers Act compliance knowledge, experience or training."[63] After its 2008 examination, the OCIE Staff expressed "its concern whether MPM's designated CCO was sufficiently knowledgeable regarding MPM's compliance operations relative to the Advisers Act to adequately administer MPM's compliance program as its CCO."[64] Failing to heed this warning, MPM subsequently designated Damasco as its CCO "despite his lack of compliance experience and unfamiliarity with compliance requirements under the Advisers Act."[65]

This enforcement action against MPM and its principals exemplifies the SEC's focus on repeat offenders who fail to remediate identified deficiencies. As the SEC noted in its Order, Damasco and Ohm were "aware of the deficiencies" that the OCIE Staff had identified, but they "did not take adequate corrective action to prevent the failures from the 2008 examination from being repeated during the 2011 examination."[66] To resolve this action, MPM agreed to retain an independent compliance consultant for three years and to adopt and implement all of the recommendations from the consultant.[67] Damasco and Ohm also agreed to complete 30 hours of compliance training, and MPM agreed to designate a new, qualified CCO (other than Damasco).[68] The SEC issued cease-and-desist orders; censured MPM, Damasco, and Ohm; and imposed civil monetary penalties of $75,000 against MPM, $50,000 against Damasco and $50,000 against Ohm.[69]

Meanwhile, another Compliance Rule case, which the SEC filed in federal court in 2012, abruptly ended in 2013 when the defendants defaulted. In December 2012, the SEC charged GEI Financial Services, Inc., a hedge fund in Chicago, Illinois, along with its CEO Norman Goldstein and CCO Laurie Gatherum, with fraud and various compliance violations.[70] Initially, GEI, Goldstein and Gatherum denied all of the charges,[71] but after their counsel withdrew, none of the defendants retained new counsel, appeared in the case or responded to letters, emails and discovery requests from the SEC. As a result, and with the court's permission, on July 1, 2013, the SEC moved for a default judgment.[72] GEI had many serious problems, but with regard to the Compliance Rule, the SEC alleged:

> GEI Financial's compliance program consisted only of excerpts of Section 13 of the Securities Exchange Act of 1934 and an unsigned policy prohibiting insider trading. GEI Financial had no other written compliance policies and procedures, a code of ethics, or internal controls to prevent violations of the Advisers Act. Gatherum [the CCO] did not annually review or update a code of ethics or compliance policies and never discussed these policies with GEI Financial's employees.[73]

The SEC further alleged:

> SEC compliance examiners inspected GEI Financial in 2008 and cited the company for not having written compliance policies and procedures. Defendants promised to fix these deficiencies, but a December 2011 through January 2012 on-site visit revealed the same problems.[74]

On July 30, 2013, the federal court in Chicago allowed the SEC's motion, entered a default judgment against GEI, Goldstein, and Gatherum, and provided the requested relief: a permanent injunction barring violations of the Advisers Act, disgorgement of "ill-gotten gains" with interest and civil monetary penalties.[75] Specifically, the court held the defendants jointly and severally liable for more than $162,000 in disgorgement and interest, which was the sum of (i) more than $92,000 in excessive fees, (ii) nearly $55,000 in improper capital withdrawals, and (iii) about $14,000 in interest.[76] In addition, the court imposed civil monetary penalties of $450,000 against GEI, $300,000 against Goldstein and $150,000, against Gatherum.[77] The SEC characterized these Tier 3 penalties as "significant" yet justified by the "high degree of scienter."[78] Although the penalties against Goldstein and Gatherum represented maximum penalties (for two violations and one violation, respectively), based on the statutory caps in place for 2009, the SEC emphasized that it did not seek "the maximum amount permitted *for each* violation," which the law permits.[79]

These enforcement actions arising from violations of the Compliance Rule—whether focused on issues concerning the adequacy of compliance manuals as in the actions against Equitas and GEI or the qualifications of compliance staff as in the action against MPM—demonstrate the importance of effectively remediating all compliance-related deficiencies, particularly those that the OCIE Staff identifies during its examinations. Investment advisers can expect the Enforcement Division Staff to follow-up, if compliance problems persist.

C. The Custody Rule

Rule 206(4)-2 under the Advisers Act, also known as the Custody Rule, aims to protect advisory clients from the misuse or misappropriation of their funds and securities.[80] The rule has been a top enforcement priority because, according to the SEC, "[t]he heart of the relationship between advisers and their customers is the safety of client assets."[81] Many investment advisers (perhaps, most of them) fulfill their obligations under the Custody Rule by contracting with reputable banks or brokers to hold client assets in custodial accounts. But that is not universally true, and some advisers may be deemed to have legal custody, even without physical custody, because they have access to funds or securities held by third-parties. The SEC advises potential investors in hedge funds to research "how a fund's assets are kept safe."[82]

Based on its National Examination Program, the SEC has observed what it considers to be "widespread and varied non-compliance with elements of the Custody Rule."[83] More than 140 examinations revealed "significant deficiencies," including many "custody-related issues."[84] The SEC has grouped these issues into four broad categories: (1) failure by an adviser to recognize that it had "custody" as defined by the rule; (2) failure to comply with the rule's "surprise exam" requirement; (3) failure to comply with the "qualified custodian" requirement, and (4) failure to comply with the audit approach for "pooled investment vehicles."[85] These examinations led, in numerous instances, to referrals for administrative enforcement actions, and the SEC recently announced the settlement of three such cases.

In *In the Matter of Knelman Asset Management Group, LLC and Irving P. Knelman*,[86] Knelman Asset Management Group (KAMG), a registered investment adviser in Minneapolis, Minnesota, and Irving Knelman, the managing director, CEO and CCO of KAMG, advised Rancho Partners I, LLC (Rancho), a pooled investment vehicle and fund of private equity funds, but KAMG and Knelman failed to arrange for annual surprise examinations of Rancho's assets or, alternatively, to provide Rancho's members with audited financial statements from an independent auditor.[87] As the managing member of Rancho, KAMG was deemed to have custody of its assets, but a qualified custodian did not hold those assets to assure safekeeping. Further, the assets were not subject to any surprise examinations, and Rancho's members did not receive audited financial statements. Although the OCIE Staff had identified Custody Rule deficiencies following an examination in 2005, KAMG did not promptly fix all of these problems; indeed, the OCIE Staff found many of the same problems, during a subsequent examination in 2010.[88]

As is often the case, these violations of the Custody Rule related to, and even overlapped with, violations of the Compliance Rule. Detailing "KAMG's compliance failures," the SEC found the following:

> KAMG's policies and procedures were not reasonably designed to prevent violations of the custody rule. The firm's compliance manual did not

> acknowledge that KAMG had custody over Rancho's assets. Thus, it had no written policies and procedures to ensure that it met the requirements of the custody rule regarding Rancho's assets.[89]

These compliance problems arose, at least in part, from KAMG's reliance on Knelman as the firm's CCO, even though "he had no relevant experience in the compliance industry and failed to undergo any compliance training to become knowledgeable about that position."[90] The SEC faulted Knelman for failing "to establish written policies and procedures reasonably designed to prevent violations of the Advisers Act as they related to custody over Rancho's assets."[91]

To resolve this enforcement action, KAMG agreed to continue working with an independent compliance consultant, whom KAMG had retained at its own expense during the SEC investigation, for two more years. It also agreed to designate a new, qualified CCO, and provide a copy of the Order to Rancho's members, other advisory clients and any prospective clients. Knelman agreed to complete 30 hours of compliance training concerning the Advisers Act. In addition, the SEC issued cease-and-desist orders, censured KAMG and barred Knelman from serving as the CCO of any investment adviser or broker-dealer for three years. It imposed civil monetary penalties of $60,000 against KAMG and $75,000 against Knelman.

In *In the Matter of GW & Wade, LLC*, the SEC found that GW & Wade, a registered investment adviser in Wellesley, Massachusetts, with almost $4 billion in assets under management, failed to comply with the Custody Rule.[92] GW & Wade employed "several types of client arrangements that gave it access to, and, in certain cases, the ability to transfer, client funds for which it did not have proper safeguards as a custodian."[93] For example, GW & Wade maintained pre-signed letters of authorization from over 900 clients that allowed the firm to transfer client funds, an improper practice that left those funds vulnerable to fraud and loss.[94] The SEC also deemed GW & Wade to have custody over assets in accounts for which it had been authorized by clients to write checks or possessed log-in information for clients (user names and passwords).[95] Despite having custody, GW & Wade failed to obtain surprise inspections of these assets or to comply with other requirements of the Custody Rule.

As part of the settlement, GW & Wade agreed to retain an independent compliance consultant at the firm's expense for two years, to have the consultant conduct a comprehensive review of all compliance policies and procedures, and to follow all of the recommendations from the consultant.[96] By the time of the settlement, GW & Wade had already remediated its Custody Rule deficiencies but agreed to make disclosures to its clients about the situation. The SEC issued a cease-and-desist order, censured GW & Wade and ordered that it pay $250,000 in civil monetary penalties.[97]

In *In the Matter of Further Lane Asset Management, LLC, Osprey Group, Inc. and Jose Miguel Araiz*,[98] Further Lane Asset Management, LLC (FLAM), a registered adviser in New York, New York, which advised three hedge funds, maintained custody of client assets, but it failed to arrange for surprise inspections or to ensure that a qualified custodian provided quarterly account statements.[99] Following an examination by the OCIE Staff in 2003, FLAM was advised that, "if it were deemed to have custody of a client's assets," it would be required to comply with all aspects of the Custody Rule.[100] FLAM failed to follow that guidance, however. Although FLAM had custody over substantial assets, both through physical possession and also by virtue of its position as the general partner of the three hedge funds, FLAM and Jose Miguel Araiz, its CEO and CCO, "failed to form a reasonable belief that a qualified custodian was sending account statements to fund investors at least quarterly."[101] For a three-year period from 2008 through 2011, they also failed to subject assets to annual surprise examinations.[102] As with the action against KAMG, the custody problems at FLAM closely related to more general compliance failures.[103]

In connection with the most recent examination by the OCIE Staff, FLAM retained two independent compliance consultants, and since that examination, FLAM hired a new CCO, who conducted a comprehensive review of compliance policies and procedures.[104] To settle the enforcement action, FLAM agreed to continue working with these consultants for two more years. It also agreed to revise its organizational structure in order to separate the position of CCO from all other officer positions. As in the other actions, FLAM agreed to notify all of its clients concerning the Order.[105] The SEC also issued cease-and-desist orders against FLAM and Araiz and censured both respondents.[106] Based upon other violations (not violations of the Custody Rule), FLAM, Araiz and a related entity agreed to pay almost $350,000 in disgorgement and interest.[107] As the 99 percent owner of FLAM, Araiz was held individually responsible for the serious violations at issue. He was suspended from associating with, or serving as an officer, director or employee of, any investment adviser or broker-dealer, and he must pay a civil monetary penalty of $150,000.[108]

As noted above, all three of these Custody Rule actions involved investment advisers (and related individuals) who had been notified in the past by the OCIE Staff of significant deficiencies yet failed to take appropriate measures to correct those problems. Not surprisingly, that is a recipe for trouble with the Enforcement Division Staff. When it announced the settlements in these three cases, the SEC warned: "These firms failed to comply with their custody rule obligations, and other firms who hold client assets should take notice that we will vigorously enforce such requirements."[109]

D. Valuation Issues

Late last year, Bruce Karpati, then-Chief of the Asset Management Unit, addressed the Regulatory Compliance Association to speak about "current hedge fund enforcement priorities."[110] Among the topics that Karpati addressed was how hedge funds value their assets under management:

> Because hedge fund managers are compensated by both management fees and performance fees, the manager has incentives to overprioritize compensation. For example, the temptation to overvalue assets to boost compensation has emerged repeatedly in enforcement cases. The AMU is focused on detecting fraudulent or weak valuation practices—including lax valuation committees and the use of side pockets to conceal losing illiquid positions—and the failure to follow a fund's stated valuation procedures.[111]

That valuation message echoed advice that the SEC gives to potential investors in hedge funds:

> Understand how a fund's assets are valued. Hedge funds may invest in highly illiquid securities that may be difficult to value. Moreover, many hedge funds give themselves significant discretion in valuing illiquid securities. You should understand a fund's valuation process and know the extent to which a fund's securities are valued by independent sources. Valuations of fund assets will affect the fees the manager charges.[112]

From the SEC's perspective, like compliance failures, even minor valuation concerns can lead to far more serious problems, including fraud on investors.[113]

By the time Karpati raised a red flag concerning valuation issues, the SEC had already charged a hedge fund adviser, Yorkville Advisors, LLC, along with two of its executives, President Mark Angelo and chief financial officer (CFO) and COO Edward Schinik, with allegedly scheming to overvalue assets under management and exaggerate investment returns, thereby hiding losses from investors and boosting fees for themselves.[114] Yorkville and its executives fought back, and that litigation is ongoing in the federal court in New York.

On August 2, 2013, the court denied Yorkville's motion to dismiss the SEC's complaint. Although the court concluded that "[s]everal of the SEC's individual allegations fail[ed] to adequately state a securities fraud violation with the particularity required by Rule 9(b)," it nevertheless ruled that certain allegations were sufficiently particularized to sustain the SEC's securities fraud claims.[115] For example, based solely on the complaint, the court ruled that the SEC adequately alleged that Yorkville had misrepresented the age of certain convertibles and, as a result, the value of those investments.[116] (The court ruled that many other allegations fell short, however.[117]) On September 20, 2013, the court denied the SEC's motion for leave to amend its complaint, as an unnecessary and improper "attempt[] to supplement the SEC's previous claims with additional allegations of materiality and scienter, apparently to broaden its theory of liability."[118] Because the court denied Yorkville's motion to dismiss, there was no reason to allow the SEC's motion for leave; the SEC could simply proceed with its action against Yorkville. The case is now moving forward into discovery.

Meanwhile, in an unusual and high-profile enforcement action, the SEC charged eight directors of Morgan Keegan & Co., a mutual fund adviser (which is now part of Raymond James), with failing to ensure that mutual fund assets were properly valued, in violation of Rule 38a-1 under the Investment Company Act of 1940.[119] According to the SEC, the funds at issue had invested in risky securities backed by subprime mortgages and "fraudulently overstated the value of their securities as the housing market was on the brink of financial crisis in 2007."[120] After securing a $200 million settlement with the funds' managers,[121] the SEC turned its attention to the funds' directors, concluding that the individual directors breached fiduciary duties, which they owed to fund investors, to ensure fair and accurate valuations of securities.

> The Directors did not specify a fair valuation methodology pursuant to which securities were to be fair valued. Nor did they continuously review how each issue of security in the Funds' portfolios was being valued. The Directors delegated their fair value responsibility to a valuation committee without providing meaningful substantive guidance on how fair valuation determinations should be made. The fund directors then made no meaningful effort to learn how fair values were being determined. They received only limited information about the factors involved with the funds' fair value determinations, and obtained almost no information explaining why particular fair values were assigned to portfolio securities.[122]

When it comes to fund management, delegation will not discharge directors' fiduciary duties, rather directors must provide guidance on valuation and stay informed. In the end, all of the directors settled, and the SEC issued cease-and-desist orders against each of them individually.[123]

In another follow-on action against an individual fund manager, the SEC charged Brian Williamson, the former manager of a fund of private equity funds at Oppenheimer & Co., with making misleading statements about asset valuation and fund performance, in violation of Section 206(4) of the Advisers Act, Rule 206(4)-8 and other federal securities laws.[124] Oppenheimer had previously settled related charges and agreed to pay $2.8 million to the SEC.[125] In announcing the administrative enforcement action against Williamson, the SEC stressed that "[i]nterim valuations are especially important when used to raise funds in the private equity industry" and, therefore, that "[p]rivate fund managers must provide investors with accurate disclosures about valuation methodologies as well as fund fees and expenses so they can make fully informed investment choices."[126]

With regard to Williamson in particular, the SEC alleged that he misrepresented to investors and prospective investors that his fund valuations were based on estimates by the underlying fund managers (not his own estimates, which created the misleading impression of increased performance).[127] Like the court case against Yorkville, the administrative proceeding against Williamson is still pending. The next hearing is scheduled for January 13, 2014, before Chief Administrative Law Judge (ALJ) Brenda Murray.

In yet another valuation matter, the SEC charged George R. Jarkesy, Jr. and Thomas Belesis with perpetrating an alleged fraud against their hedge fund investors.[128] Jarkesy was the portfolio manager of John Thomas Capital Management, LLC (JTCM), an unregistered investment adviser to two hedge funds, and Belesis served as CEO of John Thomas Financial, Inc. (JTF), which executed trades for the funds and also acted as a placement agent. The SEC claims Jarkesy and Belesis defrauded investors in two ways. The first aspect of their fraud involved valuation:

> Jarkesy and his firm, John Thomas Capital Management, inflated the valuations of the funds' assets, causing the value of investors' shares to be overstated and his management and incentive fees to be increased.[129]

The second aspect involved the improper relationship between the adviser (JTCM and Jarkesy) and the broker (JTF and Belesis):

> Jarkesy led investors to believe that as manager of the funds, he was solely responsible for all investment decisions. However, Belesis sometimes supplanted Jarkesy as the decision maker and directed some investments from the hedge funds into a company in which his firm was heavily invested. Belesis also bullied Jarkesy into showering excessive fees on John Thomas Financial even in instances where the firm had done virtually nothing to earn them.[130]

Belesis and JTF settled with the SEC.[131] The final Order recites that Belesis and JTF "aided, abetted and caused" breaches of fiduciary duties that Jarkesy and JTCM owed to the funds.[132] It further concludes that the purported "independence" between JTF and JTCM was "untrue" and that Jarkesy and JTCM used fund assets to pay Belesis and JTF "significant amounts for services that had little or no direct value to the funds."[133] The SEC censured both Belesis and JTF and issued cease-and-desist orders against them; it also barred Belesis from associating with, or working for, any investment adviser or broker-dealer and also from participating in any penny stock offering.[134] In terms of financial consequences, the SEC ordered Belesis to disgorge nearly $400,000 and pay a civil monetary penalty of $100,000.[135] It also ordered JTF to pay a penalty of $500,000.[136]

Meanwhile, the proceeding against Jarkesy and JTCM is moving ahead. Jarkesy and JTCM had asked for an order compelling the production of all "exculpatory" evidence (which the government would be obligated to turn over in a criminal prosecution) and for a continuance to review the "voluminous" documents that the SEC has produced. That request was denied. Jarkesy and JTCM then petitioned for interlocutory review of the discovery, but that petition was recently denied as well.[137] The next step, presumably, will be setting a new date for the evidentiary hearing on the pending charges.

The outcome of these valuation actions—whether scheduled for a hearing before an ALJ, set for trial in federal court or headed for settlement—will likely pave the way for yet more SEC enforcement activity. Although allegations that investment advisers have fraudulently over-valued assets can be difficult to prove, the SEC has identified such charges as central to its enforcement mission and investor protection. When advisers over-value assets, they misrepresent fund performance and often collect excessive fees from their investors.

II. The Supreme Court's Decision on the Statute of Limitations

In *Gabelli v. SEC*,[138] the Supreme Court issued a much anticipated decision on the statute of limitations for civil enforcement actions in which the SEC seeks monetary remedies. The appeal arose from a case in which the SEC alleged that, almost 10 years earlier, mutual fund managers had allowed an investor to engage in "market timing" activities. Defendants Marc Gabelli, the portfolio manager of Gabelli Global Growth Fund (GGGF), and Gary Albert, the COO of Gabelli Fund, LLC, which served as GGGF's adviser, moved to dismiss, arguing that the SEC had waited too long to bring its case.

On appeal, the Supreme Court unanimously ruled for Gabelli and Alpert, holding that the "discovery rule" does not extend the five-year statute of limitations set by 28 U.S.C. § 2462, which broadly applies to many penalty provisions under federal law, including those for SEC enforcement actions. The Court reasoned that, "[u]nlike a private party who has no reason to suspect fraud, the SEC's very purpose is to root it out, and it has many legal tools at hand to aid in that pursuit."[139] Thus, the federal court in New York properly dismissed as time-barred the SEC's claims for financial penalties.

Gabelli is significant because it rejected the SEC's position (which was widely criticized by amici curiae, including the Securities Industry and Financial Markets Association), overturned prior precedent including *SEC v. Tambone*,[140] and limited how far back in time the SEC may reach in certain cases. It should be noted, however, that *Gabelli* addressed only SEC enforcement actions for monetary penalties, fines or forfeiture, and not actions for disgorgement or injunctive relief, which are "equitable remedies" and remain subject to the discovery rule. In its complaint against Gabelli and Alpert, the SEC also sought disgorgement and injunctive relief, and the district court ruled those claims were timely because Section 2462 expressly refers to actions for "the enforcement of any civil fine, penalty or forfeiture." Gabelli and Alpert did not challenge that decision before the Supreme Court.[141]

The implications of *Gabelli* are currently being disputed in *In the Matter of Timbervest, LLC et al.*, where the SEC has alleged that Timbervest, a registered investment adviser in Atlanta, Georgia, which manages approximately $1.2 billion in timber-related investments, engaged in unauthorized and undisclosed transactions in 2006 and 2007 that benefitted Timbervest and its principals at the expense of its clients.[142] Timbervest has denied those allegations and argued that the SEC's enforcement action, which seeks civil monetary penalties, runs afoul of the Supreme Court's ruling in *Gabelli*, because the SEC has sought to reach back to transactions that occurred more than five years ago. Recently, Chief ALJ Murray allowed Timbervest's motion for leave to file a dispositive motion, which may present the issue for decision and, possibly, appeal to the Commission.

III. Whistleblowers' Activities and Protections

The close of the 2013 fiscal year (which ended for the SEC on September 30, 2013) marked the end of the second full year for the Office of the Whistleblower. In its 2013 annual report, the Office of the Whistleblower reported that it received a total of 3,238 tips and complaints, up only slightly from 3,001 tips and complaints during the prior year.[143] These whistleblowers hailed from all 50 states, the District of Columbia, Puerto Rico, Guam, the US Virgin Islands and 55 foreign countries.[144] Just like the tips in 2012, the most common complaint categories in 2013 raised familiar issues: corporate disclosures and financials (17 percent), offering fraud (17 percent), and market manipulation (16 percent).[145]

Since its inception, the Office of the Whistleblower has awarded "bounties" to six whistleblowers: one in fiscal year 2012; four in fiscal year 2013, including an award for $14 million, which is by far the largest award to date; and one (so far) in fiscal year 2014.[146] In addition, in 2013, the SEC also issued three more payments to whistleblowers from 2012 in connection with additional amounts that the SEC recouped in 2013 in the related enforcement action.[147] These payments reflect the SEC's policy of distributing awards as percentages of all funds recovered over the lives of cases, not the initial amounts alone.

It is possible that the news regarding the recent $14 million award may lead to an increased volume of tips and complaints to the SEC from whistleblowers and, as a result, an increased docket of enforcement actions by the SEC. But that sizable award is an outlier: the five other whistleblower awards have been for dramatically lower amounts: $150,000,[148] $50,000,[149] and a combined award of $25,000 to three whistleblowers.[150] Beyond the dollar amounts of these awards, there is very little public information about the underlying matters, due to confidentiality restrictions. What did the whistleblowers tell the SEC, and how did that information assist with enforcement actions? With regard to the $14 million award announced on October 1, 2013, the SEC has not described the substance of the tip, except to say that the information led to an enforcement action that "recovered substantial investors funds."[151] Similarly, with regard to the award of $150,000 announced on October 30, 2013, the SEC simply stated that the tip "helped the agency stop a scheme that was defrauding investors."[152] The scarcity of available information raises doubts about whether these awards will have the desired effect of eliciting yet more tips from new whistleblowers.

Of particular interest to investment advisers, the SEC did reveal that the three awards announced on August 30, 2013, which totaled

$25,000, were for tips concerning a "sham hedge fund" and that the whistleblowers stand to receive about $125,000, which would represent 15 percent of the money that the SEC hopes to collect in its enforcement action against Locust Offshore Management (LOM) and its CEO Andrey C. Hicks.[153] In late 2011, the SEC filed a civil injunctive action, alleging LOM and Hicks engaged in a scheme to mislead prospective investors about their supposed quantitative hedge fund and divert over $2.5 million of investors' money to Hicks' personal bank accounts.[154] The SEC alleged that Hicks falsely represented to potential investors that (1) he obtained degrees from Harvard University; (2) he worked for Barclays Capital, where he "grew his book nearly two-fold and expanded his group's assets under management to roughly $16 [billion]"; (3) Ernst & Young served as LOM's auditor; (4) Credit Suisse served as its prime broker and custodian; and (5) LOM was a business company incorporated under the laws of the British Virgin Islands.[155] Around the same time, the US Attorney's Office in Boston charged Hicks with committing wire fraud.[156] In the end, Hicks pleaded guilty in his criminal case, and the court sentenced him to 40 months in prison.[157] The court also entered default judgments in the SEC action against LOM and Hicks, ordering them to cease-and-desist from violating federal securities laws and holding them jointly and severally liable for disgorgement and interest in excess of $2.5 million.[158] In addition, the court ordered both LOM and Hicks to pay civil penalties of more than $2.5 million.[159]

In addition to the lack of information from the SEC regarding the substance of tips, the prospect for retaliation may also dissuade potential whistleblowers from coming forward. Over the past few years, courts have begun to wrestle with difficult questions about the scope of the anti-retaliation protections under both the Dodd-Frank Act and the Sarbanes-Oxley Act. Because these laws do not reach all tips by all persons about all illegal activity, courts must figure out which whistleblowers are, in fact, protected.

Although the SEC has interpreted the Dodd-Frank Act to protect whistleblowers who report securities fraud, whether they drop a dime to the SEC, another law enforcement agency, or an internal supervisor, the Fifth Circuit held otherwise in *Asadi v. G.E. Energy (USA), LLC.*[160] Asadi sued G.E. Energy, alleging that the company violated 15 U.S.C. § 78u-6(h) by firing him after he made an internal report about possible FCPA violations in Iraq. The district court dismissed his lawsuit (ruling Dodd-Frank did not apply "extraterritorially"), and the Fifth Circuit affirmed (ruling Asadi was not a "whistleblower" under the statute).[161] The appeals court gave no deference to the SEC's broad interpretation of the anti-retaliation provision, finding the agency's reading of the Dodd-Frank Act to be at odds with the plain terms of the statute.[162] Several federal courts have similarly ruled that the Dodd-Frank Act's anti-retaliation provision applies only to individuals who make reports to the SEC before any alleged retaliation.[163] But other federal courts have taken a broader view. In *Ellington v. Giacoumakis*, the court rejected the argument that, because Ellington did not report his concerns to the SEC until after he was fired, he did not qualify as a Dodd-Frank Act whistleblower entitled to protection from retaliation.[164] In *Rosenblum v. Thomson Reuters (Markets) LLC*, the court allowed Rosenblum's claim that he was fired for reporting to internal management (and, then, to the FBI) his concerns about distributing consumer survey data to different customers at varying times.[165] In both cases, the court deferred to the SEC's interpretation of the statute.

Despite this disagreement about the scope of the Dodd-Frank Act's anti-retaliation provision, the federal courts have agreed, so far at least, that the whistleblower protection does not apply to reports made outside the United States by employees of foreign companies (for example, about potential violations of the Foreign Corrupt Practice Act).[166] Even where a foreign employer is a wholly owned subsidiary of a foreign company traded on an exchange in the United States, an employee blows the whistle at his or her own peril. Following the principles established by the Supreme Court in *Morrison v. National Australia Bank*, courts have required whistleblowers to have at least a territorial toehold in the United States.[167]

Another open question about whistleblower protection concerns the scope of the Sarbanes-Oxley Act's anti-retaliation provision[168]

—whether it applies to an employee of a private company that contracts with a public company if the employee reports suspected wrongdoing. In *Lawson v. FMR, LLC*, the First Circuit held that employees of FMR, a private company that provided advisory services to Fidelity mutual funds, could not sue their employer for retaliation after having blown the whistle regarding suspected violations of securities laws.[169] That decision is now on appeal to the Supreme Court. Meanwhile, the Department of Labor's Administrative Review Board (ARB), which handles administrative proceedings concerning alleged retaliation under the Sarbanes-Oxley Act, held in *Spinner v. David Landau and Associates, LLC* that Section 1514A extends to "accountants employed by private accounting firms who in turn provide [Sarbanes-Oxley Act]-compliance services to publicly traded corporations."[170] Whether courts should defer to the ARB's reading of the Sarbanes-Oxley Act has been hotly contested. These critical questions may be resolved soon, because on November 12, 2013, the Supreme Court heard oral argument in *Lawson*, and its decision in that appeal is expected later this term.

IV. The SEC's First DPA with an Individual

Not every whistleblower is an innocent bystander. Some people learn first-hand about securities fraud by participating in it. The SEC recently confronted this situation in *SEC v. Berton M. Hochfeld et al.*, an emergency action against Hochfeld Capital Management, LLC (HCM), a hedge fund adviser in Stamford, Connecticut, and Berton Hochfeld, the founder and manager of HCM, for overstating the performance of Heppelwhite Fund LP and misappropriating client assets.[171] The SEC first learned about this fraud from Scott Herckis, a former administrator for Heppelwhite, who aided and abetted the misconduct by Hochfeld and HCM. After he resigned in September 2012, Herckis contacted the SEC, reported his concerns and voluntarily turned over documents. With this substantial assistance from Herckis, the SEC was able to proceed on an emergency basis, freezing both Heppelwhite's fund assets as well as Hochfeld's personal assets for use to compensate defrauded investors.

Shortly after the report by Herckis, on November 9, 2012, the SEC filed its complaint. Less than one week later, on November 14, 2012, the federal court in New York entered consent judgments against Hochfeld and HCM, ordering injunctive relief, asset freezes and the payment of disgorgement and civil monetary penalties in amounts to be determined later.[172] Since then, over the past year, the SEC has worked with counsel for Hochfeld, a court-appointed receiver for HCM and representatives of the defrauded investors "to maximize potential compensation to investors for losses they suffered as a result of Hochfeld's misconduct."[173] Based on that work, the SEC proposed, and the court adopted, a Distribution Plan, which will distribute initial payments of more than $6 million to former investors and also later payments from additional funds to be collected from the sale of Hochfeld's personal assets.[174]

At the same time, following a federal criminal investigation, the US Attorney's Office in Manhattan filed charges against Hochfeld for securities fraud and wire fraud.[175] The two-count Information alleged that Hochfeld misled investors by "direct[ing] monthly statements to be sent to Heppelwhite Fund investors that reflected the higher NAV of the Heppelwhite Fund as calculated by internal accounting records, rather than the lower NAV reflected in the books of the Prime Broker."[176] It also alleged that Hochfeld stole from investors by "withdrawing money from the Heppelwhite Fund for his own personal use."[177] Hochfeld pleaded guilty to both charges. Prosecutors recommended a sentence of six-and-one-half to eight years in prison, citing the "brazen fraud" by Hochfeld, who misappropriated client assets to pay for "extravagant material possessions and other indulgences."[178] They argued that a lengthy prison term "will deter other investment professionals like Hochfeld from exploiting their investment advisory positions and victimizing individuals who have entrusted the investment professionals to manage financial assets."[179] Ultimately, the court sentenced Hochfeld to two years in prison and three years of supervised release (which is similar to probation).[180] The court also barred Hochfeld, as a special condition of his supervised release, from working in the financial services industry.[181]

But what about Herckis, the whistleblower who aided and abetted Hochfeld's fraud but, then, brought that wrongdoing to the SEC's attention back in late 2012? More than one year later, on November 12, 2013, the SEC announced that it had entered a deferred prosecution agreement (DPA) with Herckis.[182] This DPA is the first between the SEC and an individual, and according to the SEC, it represents an important tool in the enforcement arsenal:

> Deferred prosecution agreements (DPAs) encourage individuals and companies to provide the SEC with forthcoming information about misconduct and assist with a subsequent investigation. In return, the SEC refrains from prosecuting cooperators for their own violations if they comply with certain undertakings.[183]

Pursuant to his DPA concerning the fraud against Heppelwhite investors, Herckis admitted and accepted complete responsibility for aiding and abetting violations of securities laws "by improperly transferring Fund assets to the Fund's manager and by preparing and providing materially overstated account statements to Fund investors."[184]

The DPA provides that, for five years, Herckis cannot serve as an administrator for any fund (a position for which he had no prior experience in the first place) or work in any other capacity for any investment adviser.[185] Herckis must fully cooperate with all related investigations and enforcement actions by the SEC, including by providing documents, submitting to interviews, and possibly testifying in court.[186] He also agreed to disgorge more than $50,000 in fees that he received from Heppelwhite.[187] In exchange, the SEC agreed as follows:

> Subject to the full, truthful, and continuing cooperation of [Herckis] with all obligations, prohibitions and undertakings of the Agreement during the Deferred Period [from November 8, 2013 to November 8, 2018], the Commission agrees not to bring any enforcement action or proceeding against [Herckis] arising from the Investigation, after the conclusion of the Deferred Period.[188]

The Agreement binds only the SEC (but no other law enforcement agency or self-regulatory organization), and it relates only to potential enforcement actions arising from the fraud at Heppelwhite (but no other violations of law).[189] If during the Deferred Period, Herckis complies with his obligations and refrains from any further misconduct, the SEC will not bring an enforcement action against him arising from this case.

The DPA between the SEC and Herckis marks an important milestone for the SEC, which in recent years has increasingly relied on tactics traditionally associated with prosecutors. Since announcing its new Cooperation Initiative in 2010,[190] the SEC has entered into DPAs,[191] and their procedural cousin, non-prosecution agreements.[192] It now appears that, under the leadership of Chairman White, this enforcement trend will continue, and even expand, with more agreements between the SEC and individuals who are able to provide critical cooperation to the Enforcement Division Staff.[193]

V. Conclusion

The SEC and its Enforcement Division now has new leadership, with senior management drawn largely from the ranks of former federal prosecutors. Chairman White, Co-Directors Canellos and Ceresney and others in the Enforcement Division consider the SEC to be a critical and aggressive law enforcement agency. Given that shared perspective, they can be expected to continue certain recent trends: bringing high-profile charges and trying enforcement actions in federal court and, at the same time, pursuing minor violations and sending the message that basic compliance is critical.

Enforcement activity will undoubtedly focus, as it has in the past several years, on investment advisers, who collectively manage many trillions of dollars in assets. The OCIE will continue to leverage the National Examination Program to identify pervasive compliance failures and other common problems, particularly with newly registered advisers, and the Enforcement Division will move swiftly to make examples of advisers who do not promptly and completely remediate those issues that examinations identify. As in the past year, when examinations revealed widespread failures to comply with the Custody Rule, future examinations of investment advisers will also help the SEC to establish, at an institutional level, its top enforcement priorities.

Further, forthcoming court decisions about whistleblower protections, including the appeal to the Supreme Court in *Lawson*, will influence who brings alleged misconduct to the attention of the SEC, from where, against whom and about what. The Office of the Whistleblower will keep trying to solicit as many tips as possible, and where appropriate, the Enforcement Division may enter into more deferred prosecution agreements with tipsters to secure their cooperation in enforcement actions.

Investment advisers of all sizes, whether registered or not, must stay on top of these many developments to avoid becoming yet another statistic in the SEC's enforcement activity for fiscal year 2014.

Notes

1. Pub. L. 111-203, 124 Stat. 1376 (2010).

2. *See* "Implementing Dodd-Frank Wall Street Reform and Consumer Protection Act — Accomplishments," SEC Dodd-Frank Spotlight, available at *http://www.sec.gov/spotlight/dodd-frank/accomplishments.shtml*.

3. *See Rules Implementing Amendments to the Investment Advisers Act of 1940,* Final Rule, Rel. No. IA-3221 (June 22, 2011), 76 Fed. Reg. 42950 (amending 17 C.F.R. Parts 275 and 279).

4. *See* "SEC's Enforcement Program Continues to Show Strong Results in Safeguarding Investors and Market," Press Release 2012-227 (Nov. 14, 2012) ("Building on last year's record results, the Securities and Exchange Commission today announced that it filed 734 enforcement actions in the fiscal year that ended Sept. 30, 2012, one shy of last year's record of 735."), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171485830*. The SEC claims that, as of November 7, 2013, it has brought charges against 164 entities and individuals arising from the financial crisis. *See* "SEC Enforcement Actions: Addressing Misconduct That Led To or Arose From the Financial Crisis," available at *http://www.sec.gov/spotlight/enf-actions-fc.shtml*.

5. *See* "Mary Jo White Sworn in as Chair of SEC," Press Release 2013-56 (Apr. 10, 2013), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171514548#.Uo-83cSkrzM*.

6. *See* "Enforcement Director Robert Khuzami to Leave SEC," Press Release 2013-3 (Jan. 9, 2013), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171513652#.Uo-9O8SkrzM*.

7. *See* "George Canellos and Andrew Ceresney Named Co-Directors of Enforcement," Press Release 2013-67 (Apr. 22, 2013), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171514832#.Uo-9g8SkrzM*.

8. *See id.*

9. *See* "Bruce Karpati, Chief of Enforcement Division Asset Management Unit, to Leave SEC After 12 Years," Press Release 2013-85 (May 9, 2013), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171514274#.Uo-9vcSkrzM*.

10. *See* "Julie M. Riewe and Marshall S. Sprung Named Co-Chiefs of Asset Management Unit," Press Release 2013-118 (July 1, 2013), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171605987#.Uo-99cSkrzM*.

11. *See* David F. Marcus & Sara E. Gilley, "The Changing Nature of SEC Enforcement Actions" (Oct. 8, 2013) (reporting a 26% decline in the rate of new enforcement actions by the SEC during the first nine months of fiscal year 2013 (from October 1, 2012 to June 30, 2013) as compared to the same period in fiscal year 2012), available at *http://www.cornerstone.com/getattachment/0f99342c-a62d-4a18-b889-9c0e2468ec8b/The-Changing-Nature-Of-SEC-Enforcement-Actions.aspx*. The SEC has not yet released its year-end enforcement statistics for fiscal year 2013, which ended on September 30, 2013.

12. Morvillo Abramowitz Grand Iason & Anello PC, "SEC Enforcement Data Analyses" (Oct. 2013) at 1, available at *http://www.maglaw.com/events/speaking-engagements/00076/_res/id=Attachments/index=0/MAGIA%20SEC%20Report.pdf*; *see id.* at 5 (comparing Morvillo's and the SEC's methodologies for tracking enforcement actions). Morvillo's database only includes cases filed after January 1, 2013, and as noted above, the SEC has not yet released complete enforcement statistics for fiscal year 2013.

13. *See* SEC v. Rajat Gupta et al., No. 11-cv-7566 (S.D.N.Y. July 23, 2013).

14. *See* SEC v. Mark Cuban, No. 08-cv-2050-D (N.D. Tex. Oct. 16, 2013).

15. *See In the Matter of Steven A. Cohen*, Inv. Adv. Act Rel. No. 3634 (July 19, 2013); *see also* "SEC Charges Steven A. Cohen with Failing to Supervise Portfolio Managers and Prevent Insider Trading," Press Release 2013-129 (July 19, 2013), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370539726923*.

16. *See* SEC v. Scott London et al., No. 13-cv-2558-RGR (C.D. Cal. Aug. 7, 2013).

17. *See* Chairman Mary Jo White, "Deploying the Full Enforcement Arsenal," Remarks at Council of Institutional Investors (Sept. 26, 2013), available at *http://www.sec.gov/News/Speech/Detail/Speech/1370539841202*; Chairman Mary Jo White, "The Importance of Trials to the Law and Public Accountability," Remarks at 5th Annual Judge Thomas A. Flannery Lecture (Nov. 14, 2013), available at *http://www.sec.gov/News/Speech/Detail/Speech/1370540374908*.

18. *See* White, "Importance" (Nov. 14, 2013), *supra* n.17.

19. *See id*.

20. *See* White, "Deploying" (Sept. 26, 2013), *supra* n.17.

21. No. 12-cv-5027 & No. 12-cv-5028 (S.D.N.Y. Sept. 16, 2013).

22. *See* "Court Enters Final Judgment by Consent Against SEC Defendants Philip A. Falcone, Harbinger Capital Partners Offshore Manager, L.L.C., Harbinger Capital Partners Special Situations GP, L.L.C., and Harbinger Capital Partners LLC," Litig. Rel. No. 22831A (Oct. 2, 2013), available at *http://www.sec.gov/litigation/litreleases/2013/lr22831a.htm*.

23. *See* In the Matter of JPMorgan Chase & Co., AP File No. 3-15507 (Sept. 19, 2013) (including agreed statement of facts as Annex A); *see also* "JPMorgan Chase Agrees to Pay $200 Million and Admits Wrongdoing to Settle SEC Charges," Press Release 2013-187 (Sept. 19, 2013), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370539819965*.

24. *See* 17 C.F.R. § 242.105.

25. *Short Selling in Connection with a Public Offering*, Final Rule, Rel. No. 34-56206 (Aug. 6, 2007), 72 Fed. Reg. 45094, 45095-96 (Aug. 10, 2007); *see also* "Rule 105 of Regulation M: Short Selling in Connection with a Public Offering," National Examination Program Risk Alert, Vol. III, Issue 4 (Sept. 17, 2013) at 1 ("A fundamental goal of Rule 105 ... is protecting the independent pricing mechanisms of the securities markets so that offering prices result from the natural forces of supply and demand unencumbered by artificial forces.").

26. *See* National Examination Program Risk Alert (Sept. 17, 2013), at Appendix B (listing settled actions).

27. Chairman Mary Jo White, "Remarks at the Securities Enforcement Forum" (Oct. 9, 2013) (discussing the "broken windows approach" and stating that "[i]nvestors ... want someone who understands ... that the smallest infractions are very often just the first step toward bigger ones down the road"), available at *http://www.sec.gov/News/Speech/Detail/Speech/1370539872100*.

28. *See* "SEC Charges 23 Firms with Short Selling Violations in Crackdown on Potential Manipulation in Advance of Stock Offerings," Press Release 2013-182 (Sept. 17, 2013), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370539804376*.

29. *Id*.

30. *Id*.

31. *See, e.g.*, In the Matter of JGP Global Gestao de Recursos, AP File No. 3-15479 (Sept. 16, 2013) (total of more than $3 million in disgorgement and penalties for three violations by an exempt adviser based in Rio, Brazil, with $1.2 billion in assets under management); In the Matter of Manikay Partners, AP File No. 3-15488 (Sept. 16, 2013) (total of more than $2.5 million in disgorgement and penalties for one violation by a registered adviser in New York with $1.5 billion in assets under management); In the Matter of Deerfield Management Co., LP, AP File No. 3-15477 (Sept. 16, 2013) (total of more than $2.5 million for six violations by a registered adviser in New York with $3 billion in assets under management).

32. *See, e.g.*, In the Matter of Merus Capital Partners, AP File No. 3-15490 (Sept. 16, 2013) (disgorgement of $8,402 and a penalty of $65,000 for three violations by a proprietary trading firm in New York that invests its own capital); In the Matter of Talkot Capital, AP File No. 3-15484 (Sept. 16, 2013) (disgorgement of $17,640 and a penalty of $65,000 for one violation by a registered adviser in Sausalito, California, with more than $150 million in assets under management); In the Matter of Soundpost Partners, LP, AP File No. 3-15482 (Sept. 16, 2013) (disgorgement of $45,135 and a penalty of $65,000 for two violations by an exempt adviser in New York with about $65 million in assets under management).

33. White, "Remarks" (Oct. 9, 2013), *supra* n.27.

34. Press Release 2013-182, *supra* n.28.

35. National Examination Program Risk Alert (Sept. 17, 2013), *supra* n.26, at 4.

36. *See* White, "Remarks" (Oct. 9, 2013), *supra* n.27 (explaining the importance of pursuing all types of wrongdoing, "even violations of prophylactic rules with no intent requirement, such as the series of Rule 105 cases that we recently brought" and discussing the goal of streamlining investigations in Rule 105 cases); *see also* 72 Fed. Reg. at 45094 (Aug. 10, 2007).

37. Only one of the recent Rule 105 actions included charges against an individual. *See* In the Matter of M.S. Junior, Inc., Swiss Capital Holdings, Inc. and Michael Stango, AP File No. 3-15480 (Sept. 16, 2013). The SEC brought an enforcement action against M.S. Junior, a commercial real estate company, which was not a registered investment adviser, and in the same proceeding, it also brought charges against Michael Stango, the company's owner, principal, and CEO, who was solely "responsible for the trading activity," including 13 violations of Rule 105 between December 2010 and July 2011. As part of its settlement, the SEC held M.S. Junior and Stango jointly and severally liable for a total of about $425,000 in disgorgement, interest and penalties. It also issued cease-and-desist orders against both M.S. Junior and Stango.

38. *See* 17 C.F.R. § 275.206(4)-7.

39. "SEC Sanctions Three Firms Under Compliance Program Initiative," Press Release 2013-226 (Oct. 23, 2013)

(statement of Ceresney), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370540008287*.

40. White, "Remarks" (Oct. 9, 2013), *supra* n.27.

41. *Id*.

42. Press Release 2013-226, *supra* n.39 (explaining that the purpose of the Compliance Program Initiative is for the SEC "to address repeated compliance failures that may lead to bigger problems").

43. *See In the Matter of OMNI Investment Advisers, Inc. and Gary R. Beynon*, Inv. Adv. Act Rel. No. 3323 (Nov. 28, 2011); *In the Matter of Asset Advisors*, *LLC*, Inv. Adv. Act Rel. No. 3324 (Nov. 28, 2011); *In the Matter of Feltl & Co., Inc.*, Inv. Adv. Act Rel. No. 3325 (Nov. 28, 2011); *see also In the Matter of Consultiva Internacional, Inc.*, Inv. Adv. Act Rel. No. 3441 (Aug. 3, 2012).

44. *See* Press Release 2013-226, *supra* n.39 ("After SEC examiners identified significant deficiencies, these firms did little or nothing to address them by the next examination. Firms must fix deficiencies identified by our examiners.") (statement of Bowden).

45. Inv. Adv. Act Rel. No. 3704 (Oct. 23, 2013).

46. *See id.* at 2.

47. *Id.* at 6.

48. *Id.* at 2; *see id.* at 6 ("[D]espite repeated suggestions from OCIE [S]taff, Equitas made few changes to its manual.").

49. *Id.* at 3.

50. *See id.* at 3, 8.

51. *See id*. at 7.

52. *Id.* at 8-11.

53. Inv. Adv. Act Rel. No. 3703 (Oct. 23, 2013).

54. *Id.* at 2.

55. *Id.* at 3.

56. *See id.* at 9.

57. *See id.* at 10.

58. Inv. Adv. Act Rel. No. 3702 (Oct. 23, 2013).

59. *Id.* at 2.

60. *Id.*; *see id.* at 4.

61. *See id.* at 2.

62. *See id.* at 4.

63. *Id.* at 3.

64. *Id*. at 4.

65. *Id*. at 5.

66. *Id*.

67. *See id.* at 7.

68. *See id*.

69. *See id.* at 8.

70. *See* Complaint, SEC v. GEI Fin. Servs., Inc. et al., No. 12-cv-7927 (N.D. Ill. Oct. 3, 2012); *see also* "SEC Charges Hedge Fund Managers with Defrauding Investors," Press Release 2012-206 (Oct. 3, 2012), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171485256*.

71. *See* Answer, GEI Fin. Servs., Inc., No. 12-cv-7927 (N.D. Ill. Feb. 13, 2013).

72. *See* Pltf. Mem. in Supp. of Mtn. for Default Judgment, GEI Fin. Servs., Inc., No. 12-cv-7927 (N.D. Ill. July 1, 2013).

73. *Id.* at 7 (citing Complaint ¶ 43).

74. *Id.* at 8 (citing Complaint ¶¶ 46-47); *see id.* at 16-17 (describing violations of the Compliance Rule).

75. *See* Final Judgment, GEI Fin. Servs., Inc., No. 12-cv-7927 (N.D. Ill. July 30, 2013).

76. *See id*.

77. *See id*.

78. Mot. for Final Judgment, GEI Fin. Servs., Inc., No. 12-cv-7927 (N.D. Ill. July 23, 2013) at 3-4.

79. *See id*. at 4.

80. *See* 17 C.F.R. § 275.206(4)-2, as amended.

81. "SEC Charges Three Firms with Violating Custody Rule," Press Release 2013-230 (Oct. 28, 2013) (statement by Ceresney), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370540098359*.

82. "Hedge Funds," Investor Bulletin, SEC Pub. No. 139 at 3 (Feb. 2013), available at *http://www.sec.gov/investor/alerts/ib_hedgefunds.pdf*; *see id.* ("You should inquire about where a fund's assets are held (*e.g*., whether they are held in custodial accounts at a reputable bank or broker) and whether an independent third party confirms or otherwise verifies the existence of the fund's assets.").

83. "Significant Deficiencies Involving Adviser Custody and Safety of Client Assets," National Examination Program Risk Alert, Vol. III, Issue 1 (Mar. 4, 2013) at 1; *see id.* at 5.

84. *Id*.

85. *Id.* at 3.

86. Inv. Adv. Act Rel. No. 3705 (Oct. 28, 2013).

87. *See id.* at 2.

88. *See id*. at 4.

89. *Id.* at 6.

90. *Id*.

91. *Id*.

92. Inv. Adv. Act Rel. No. 3706 (Oct. 28, 2013).

93. *Id.* at 2.

94. *Id.* at 2-3.

95. *See id.* at 3.

96. *See id.* at 5-6.

97. *See id*. at 7.

98. Inv. Adv. Act Rel. No. 3707 (Oct. 28, 2013).

99. *See id.* at 2.

100. *Id*. at 4.

101. *Id.* at 6.

102. *See id*.

103. *See id.* at 7 (finding that FLAM failed to adopt, and then to review periodically, compliance policies and procedures adequately designed to prevent violations of the Advisers Act).

104. *See id.* at 10.

105. *See id*.

106. *See id*. at 12.

107. *See id*.

108. *See id*.

109. Press Release 2013-230, *supra* n.81 (statement of Ceresney).

110. Bruce Karpati, "Enforcement Priorities in the Alternative Space," Remarks before the Regulatory Compliance Association (Dec. 18, 2012), available at *http://www.sec.gov/News/Speech/Detail/Speech/1365171492012*.

111. *Id.*

112. "Hedge Funds," Investor Bulletin (Feb. 2013) at 2.

113. *See* David W. Grimm, "Remarks to the Investment Management Institution of 2013" (Mar. 7, 2013) ("Inaccurate valuations will lead to inaccurate performance claims; inaccurate fee payments; inaccurate transactions prices and ultimately mis-pricing can muddy the integrity of the fund industry."), available at *http://www.sec.gov/News/Speech/Detail/Speech/1365171515032*.

114. *See* Complaint, SEC v. Yorkville Advisors, LLC, No. 12-cv-7728 (S.D.N.Y. Oct. 17, 2012) (charging violations of Section 206(1), (2) and (5) of the Advisers Act, Rule 206(4)-8 and other securities laws); *see also* "SEC Charges Hedge Fund Adviser and Two Executives with Fraud," Litig. Rel. No. 22410 (Oct. 17, 2012), available at *http://www.sec.gov/litigation/litreleases/2012/lr22510.htm*.

115. Mem. & Order, Yorkville Advisors, LLC, No. 12-cv-7728 (S.D.N.Y. Aug. 2, 2013) at 7-9.

116. *See id.* at 9.

117. *See id.* at 7-8.

118. Order, Yorkville Advisors, LLC, No. 12-cv-7728 (S.D.N.Y. Sept. 20, 2013) at 1-2.

119. *See* In re Matter of J. Kenneth Alderman et al., AP File No. 3-15127 (June 13, 2013).

120. "SEC Charges Eight Mutual Fund Directors for Failure to Properly Oversee Asset Valuation," Press Release 2012-259 (Dec. 10, 2012), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171486708*.

121. *See* "Morgan Keegan to Pay $200 Million to Settle Fraud Charges Related to Subprime Mortgage-Backed Securities," Press Release 2011-132 (June 22, 2011), available at *http://www.sec.gov/news/press/2011/2011-132.htm*.

122. *In the Matter of J. Kenneth Alderman, supra* n.119 at 2.

123. *See id.* at 12.

124. *See* In the Matter of Brian Williamson, AP File No. 3-15430 (Aug. 20, 2013).

125. *See* "SEC Charges Former Oppenheimer Private Equity Fund Manager with Misleading Investors about Valuation and Performance," Press Release 2013-160 (Aug. 20, 2013), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370539783859*.

126. *Id.* (statement of Riewe).

127. *See In re Matter of Brian Williamson, supra* n.124 at 2.

128. *See* In the Matter of John Thomas Capital Management Group, LLC et al., AP File No. 3-15255 (Mar. 22, 2013) (alleging violations of Sections 201(1), (2) and (4) of the Investment Advisers Act, Rule 206(4)-8 and other securities laws).

129. "SEC Charged Hedge Fund Manager and Brokerage CEO with Fraud," Press Release 2013-46 (Mar. 22, 2013), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171513444; see In the Matter of John Thomas Capital Management Group, LLC, supra* n.128 at 2 ("Jarkesy and JTCM recorded arbitrary valuations without any reasonable basis for certain of the Funds' largest holdings.").

130. Press Release 2013-46, *supra* n.129; *see In the Matter of John Thomas Capital Management Group, LLC*, *supra* n.128 at 2-3 ("Notwithstanding representations that he was 'responsible for all of the investment decisions' of the Funds, Jarkesy capitulated to Belesis' aggressive demands regarding certain investment decisions. JTCM's purported independence from JTF was a sham designed to enrich Belesis at the expense of the Funds, and to insulate him from future accusations of wrongdoing.").

131. *See In the Matter of John Thomas Capital Management Group LLC, George R. Jarkesy Jr., John Thomas Financial, Inc. and Anastosios "Tommy" Belesis*, Inv. Adv. Act Rel. No. 3732 (Dec. 5, 2012).

132. *See id.* at 2.

133. *Id*.

134. *See id.* at 9. Belesis may apply to lift these bars after one year.

135. *See id.* at 10.

136. *See id*.

137. *See In the Matter of John Thomas Capital Management Group LLC and George R. Jarkesy, Jr.*, Inv. Adv. Act Rel. No. 3733 (Dec. 6, 2013) (order denying petition for interlocutory review).

138. 133 S. Ct. 1216 (2013).

139. *Id.* at 1222.

140. 597 F.3d 436 (1st Cir. 2010) (en banc) (emphasizing the "self-concealing nature of fraud" and applying the "discovery rule" in a market timing action).

141. Even in enforcement actions for monetary remedies, like the one in *Gabelli*, the SEC may still enter agreements—known as "tolling agreements"—with investigated parties to extend the applicable five-year statute of limitations by stopping the clock for an agreed period of time.

142. AP File No. 3-15519 (Sept. 24, 2013) (charging violation of Sections 206(1) and (2) of the Advisers Act and other securities laws).

143. *See* "2013 Annual Report to Congress on the Dodd-Frank Whistleblower Program" (Nov. 15, 2013) at 8, available at *http://www.sec.gov/about/offices/owb/annual-report-2013.pdf*.

144. *Id.* at 9-10.

145. *Id.* at 8.

146. *See id.* at 14-15.

147. *Id.*

148. "SEC Rewards Whistleblower With $150,000 Payout," Press Release 2013-231 (Oct. 30, 2013), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370540158194#.Uoo8LcSkrzM*.

149. "SEC Issues First Whistleblower Program Award," Press Release 2012-162 (Aug. 21, 2012), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171483972#.Uoo8icSkrzM*.

150. "SEC Rewards Three Whistleblowers Who Helped Stop Sham Hedge Fund," Press Release 2013-169 (Aug. 30, 2013), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370539796657#.Uoo7rsSkrzM*.

151. *See* 2013 Annual Report on the Dodd-Frank Whistleblower Program, *supra* n.143 at 1.

152. Press Release 2013-231, *supra* n.148.

153. Press Release 2013-169, *supra* n.150.

154. *See* Complaint, SEC v. Hicks, et al., No. 11-cv-11888-RGS (D. Mass. Oct. 26, 2011); *see also* Litig. Rel. No. 22302 (Mar. 22, 2012), available at *http://www.sec.gov/litigation/litreleases/2012/lr22302.htm*.

155. *Id.*

156. *See* Indictment, United States v. Andrey Hicks, No. 11-cr-10407-PBS (D. Mass. Dec. 7, 2011).

157. *See* Judgment, *Hicks*, No. 11-cr-10407 (Mar. 19, 2013).

158. *See* Final Judgment as to Def. Locust Offshore Management, LLC, *Hicks*, No. 11-cv-11888-RGS (Mar. 20, 2012); Final Judgment as to Def. Andrey C. Hicks, *Hicks*, No. 11-cv-11888-RGS (Mar. 20, 2012); *see also* Litig. Rel. No. 22302.

159. *Id.*

160. 720 F.3d 620 (5th Cir. 2013).

161. *Id.* at 621

162. *Id.* at 629-30 (holding "the statute … clearly expresses Congress's intention to require individuals to report information to the SEC to qualify as a whistleblower under Dodd-Frank" and, therefore, "rejecting the SEC's expansive interpretation of the term 'whistleblower'").

163. *See, e.g.*, Wagner v. Bank of Am. Corp., No. 12-cv-00381, 2013 WL 3786643, at *5-6 (D. Colo. July 19, 2013).

164. *See* Ellington v. Giacoumakis, No. 13-cv-11791, 2013 WL 5631046 (D. Mass. Oct. 16, 2013). The court also rejected the alternative argument that because the Dodd-Frank Act was not in effect at the time when Ellington complained to his employer's compliance officer about potential securities violations of the securities laws, he was not entitled to protection under section 78u-6(h).

165. *See* Rosenblum v. Thomas Reuters (Markets) LLC, No. 13-cv-02219 (S.D.N.Y. Oct. 25, 2013).

166. *See* Liu v. Siemens AG, No. 13-cv-00317, 2013 WL 5692504 (S.D.N.Y. Oct. 21, 2013); Asadi v. G.E. Energy (USA) LLC, No. 12-cv-00345, 2012 WL 2522599 (S.D. Tex. June 28, 2012)*, aff'd on other grounds by* Asadi v. G.E. Energy (USA), LLC, 720 F.3d 620 (5th Cir. 2013). In these cases dealing with foreign tips, the whistleblowers did not make reports to the SEC. But given the number of complaints to the SEC from foreign whistleblowers, courts will certainly have to decide, in future cases, whether or not such tipsters can claim the protection of the Dodd-Frank Act's anti-retaliation provision.

167. 130 S. Ct. 2869 (2010).

168. *See* 18 U.S.C. § 1514A.

169. 670 F.3d 61, 67 (1st Cir. 2012), *cert. granted*, 2013 U.S. LEXIS 7717 (Oct. 21, 2013).

170. No. 11-111 (DOL ARB Mar. 31, 2012) (Final Order of Remand).

171. *See* Complaint, SEC v. Berton M Hochfeld et al., No. 12-cv-8202 (S.D.N.Y. Nov. 9, 2012).

172. *See* Judgment for Non-Monetary Relief against Berton M. Hochfeld, *Hochfeld*, No. 12-cv-8202 (S.D.N.Y. Nov. 9, 2012).

173. Mem. in Supp. of Mtn. to Establish Fair Fund, *Hochfeld*, No. 12-cv-8202 (S.D.N.Y. July 19, 2013) at 2.

174. *See* Pltf. Mtn. to Approve Final Distribution, *Hochfeld*, No. 12-cv-8202 (S.D.N.Y. Sept. 9, 2013); Order Granting Pltf. Mtn. to Approve Final Distribution, *Hochfeld*, No. 12-cv-8202 (S.D.N.Y. Oct. 2, 2013).

175. *See* Information, United States v. Berton Hochfeld, No. 13-cr-00021-PAC (S.D.N.Y Jan. 10, 2013).

176. *Id.* at 2.

177. *Id*.

178. Gov't Sent. Mem., *Hochfeld*, No. 13-cr-00021-PAC (S.D.N.Y. July 23, 2013) at 1.

179. *Id.* at 5.

180. *See* Judgment, *Hochfeld*, No. 13-cr-00021-PAC (S.D.N.Y. Aug. 6, 2013) at 2.

181. *See id.* at 4.

182. *See* "SEC Announced First Deferred Prosecution Agreement with Individual," Press Release 2013-241 (Nov. 12, 2013), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370540345373*.

183. *Id*.

184. Deferred Prosecution Agreement between the SEC and Respondent Scott Jonathan Herckis (Nov. 8, 2013) at 1, available at *http://www.sec.gov/news/press/2013/2013-241-dpa.pdf*.

185. *See id*. at 3.

186. *See id.* at 2-3.

187. *See id.* at 5.

188. *Id.* at 7.

189. *See id*.

190. *See* "SEC Announces Initiative to Encourage Individuals and Companies to Cooperate and Assist in Investigations," Press Release 2010-6 (Jan. 13, 2010) (noting that "similar cooperation tools have been regularly and successfully used by the Justice Department in its criminal investigations and prosecutions"), available at *http://www.sec.gov/news/press/2010/2010-6.htm*.

191. *See, e.g.*, "Tenaris to Pay $5.4M in SEC's First-Ever Deferred Prosecution Agreement," Press Release 2011-112 (May 17, 2011), available at *http://www.sec.gov/news/press/2011/2011-112.htm*.

192. *See, e.g.*, "SEC Announces Non-Prosecution Agreement with Ralph Lauren Corporation Involving FCPA Misconduct," Press Release 2013-65 (Apr. 22, 2013), available at *http://www.sec.gov/News/PressRelease/Detail/PressRelease/1365171514780*.

193. *See* White, "Importance" (Sept. 26, 2013), *supra* n.17 (discussing the importance of using the "full enforcement arsenal for the benefit of investors").