Speech

Keynote Address at the 25th Annual A.A. Sommer, Jr. Lecture on Corporate, Securities, and Financial Law

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Good evening, ladies and gentlemen, and thank you, Ben, for your generous welcome. It is a very special privilege for me to return to this lecture series in its twenty-fifth year. I should first like to recognize Ben and Amy for shepherding the Sommer Lecture into the premier event that it is today. Of course, I also should like to acknowledge the many friends and family members of Commissioner Al Sommer, about whom I will speak momentarily. But before I go further, I am sure that you appreciate that the views I express here are in my capacity as Chairman and do not necessarily reflect those of the SEC as an institution or of my fellow Commissioners.

As Ben mentioned, I last delivered this lecture as an SEC Commissioner back in 2007. Eighteen years later, I stand before you in a different role and a different era. The agency has grown, markets have evolved, and technologies that were once nascent are now reshaping how capital is raised and, unfortunately, how fraud is perpetrated. With these developments, our enforcement program has grown and become more complex, commensurate with its critical purpose of enforcing the federal securities laws.

But our three-part mission remains the same: to protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation. And the question at the heart of our mission, likewise, very much endures: how can we enforce the federal securities laws with fairness and transparency and within the boundaries set by Congress, while vigorously responding to misconduct that distorts capital raising and victimizes investors?

Al Sommer's contributions to the SEC are both vast and vital. His legacy includes efforts to eliminate fixed commissions in the brokerage industry, as well as creating and overseeing an advisory committee on corporate disclosure that resulted in the promulgation of Regulation S-K. Among other things, Regulation S-K was a much-needed rationalization of the corporate disclosure rules. Of course, following his tenure at the SEC, Al further cemented his standing in the securities industry, primarily in private practice at Morgan Lewis & Bockius, and in his roles with the accounting profession's Public Oversight Board and the American Institute of Certified Public Accountants.

On a more personal note, I very much enjoyed working with Al at the Commission in the early 1990s when I was in Chairman Richard Breeden's office. Al was an exceptional advisor—always

willing to lend his wisdom and support in a wonderful, easy-going style. After I left the agency in 1994, he continued to be a generous friend and a trusted mentor. But what strikes me most, and what feels especially relevant today, is Al's insistence that process matters. He believed, as I do, that the confidence the public bestows on regulators depends as much on the outcomes that we achieve as the manner in which we achieve them.

That conviction has guided me throughout my career. In 2007, I was happy to say at this lecture series that the Wells process had become a cornerstone of fairness. As many of you know, the Wells process is the mechanism through which the enforcement staff notifies potential respondents or defendants of any charges—and the basis for such charges—that the staff intends to recommend to the Commission. The potential respondents or defendants are then provided an opportunity to make written or video submissions to the Commission setting forth their interests and position on the subject matter of the investigation.

These "Wells submissions" provide in most cases a last opportunity for potential respondents or defendants to persuade the staff that an enforcement action, either in whole or in part as the staff intends to recommend it, is not warranted. They also provide the Commission with a different, and potentially convincing, view of the facts and law concerning the matter.

The Wells process should be viewed as an extension of due process and fundamental constitutional rights that play an integral role in protecting citizens from a powerful government agency that could become policeman, prosecutor, judge, jury, and executioner all in one. We have seen the Supreme Court focus on constitutional and due process rights in SEC matters in recent years: *Lucia v. SEC* and *Jarkesy v. SEC*, among others. I believe that this focus will continue in the future.

In my 35 years in and around the SEC, I can definitively say that Wells submissions can and do change the trajectory of enforcement actions—not in every case, of course, but in enough cases to matter. The SEC staff do not always get things right the first time, and the Wells process is a valuable procedural device that helps to guard against plain mistakes, extreme legal theories, misinformation, biases, and conflicts of interest. Tonight, I should like to return to this theme and extend it in consideration of how we can improve on and refine our enforcement processes while preserving their original purpose.

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The Enforcement Division is perhaps the most visible arm of the SEC. Its work makes headlines and can move markets. It is indispensable to our mission of rooting out fraud and manipulation because the scams that we combat can wreak devastating consequences on real people around the country, wiping out savings for retirements, down-payments, educations, and so on.

Likewise, the work of the Enforcement Division is key to ensuring that markets are honest, and that market forces—not manipulation—determine the prices of securities.

But our enforcement program is also an exercise of government power that must be tempered by fair process, good judgement, integrity, and rectitude. Its success depends substantially on the confidence of investors, market participants, and the regulated and legal communities that the SEC acts fairly and transparently in enforcing the federal securities laws. Resources are limited in any organization, including the SEC, so hard decisions must at times be made as to which matters merit an enforcement action. We must go after cases of genuine harm and bad acts, but we must view cases of benign or innocent actions differently. In the past, we have seen examples of enforcement actions in areas, such as retention of books and records, that consumed excessive Commission resources not commensurate with any measure of investor harm.

The Wells process, formally adopted in 1979, remains an essential part of our enforcement program more than forty-five years later. The Commission benefits from a robust Wells process that supplies us with the full context of the relevant facts, problems with legal theories or the use of legal authorities, potential defenses, and policy or programmatic reasons not to pursue an enforcement action. An open, informed, and thoughtful dialogue between the Division and potential respondents or defendants produces both better recommendations to the Commission and better outcomes, particularly in complex matters.

From the Commission's perspective, the process is about accuracy. We want to equip ourselves with the full context of an enforcement recommendation. We want to confirm that we are not overlooking or misconstruing important evidence or misunderstanding legal limitations on our authority. In short, we want to make sure that we get it right.

Potential respondents and defendants share a similar interest in accuracy, but, absent a Wells process, they are disadvantaged by a lack of access to the investigative record and the specific concerns of the Enforcement staff. Providing the potential respondent or defendant with information about potential charges and the key evidence that forms the basis of those potential charges is critical to due process, fairness, and transparency. For that reason, please give serious consideration to making a Wells submission when you have an opportunity.

For the Wells process to achieve its ideals, both sides must engage in good faith. My expectation is that the enforcement staff, in giving a Wells notice, will provide sufficient information for potential respondents or defendants to understand the potential charges and the evidentiary basis for those charges, such as testimony transcripts and key documents.

The staff must be forthcoming about material in the investigative file. Some materials in the file will not be available to potential respondents or defendants, and the staff must make every

effort to share information that it has gathered, while scrupulously adhering to statutory and programmatic limitations—for example, information the Commission needs to keep confidential, including whistleblower-identifying information, and matters that would implicate a parallel criminal investigation.

The staff must also be realistic about time periods for submissions, especially in long, complicated cases. Going forward, the staff will provide the other side with at least four weeks to make Wells submissions. Potential respondents and defendants should be reasonable with their requests and recognize that the staff is seeking to meet time deadlines and reach conclusions within reasonable time periods.

Both sides should engage with each other in a courteous, professional manner.

To those who would object to the government's sharing evidence with potential respondents or defendants, I ask, "Why should we not?" Our objective is to get to the truth of the matter and hold people accountable in major, federal cases for significant violations. Ours should not be a "gotcha" game.

As is the case today, when requested in a timely manner, senior enforcement leadership will meet with defense counsel before making a recommendation to the Commission. Of course, that does not necessarily mean multiple meetings.

Ordinarily the staff provides a Wells notice. But in rare instances, a Wells notice may not be practicable. In an ongoing fraud, for example, the staff may need to proceed into court quickly to prevent investor funds from being dissipated or for other emergency relief. All staff recommendations to the Commission state whether the opportunity was provided for a Wells submission or explain why not.

Today, Commissioners receive every Wells submission in settled and contested cases, and they ought to read these often very costly presentations. I was stunned in 2002 when I returned to the Commission to find that Wells submissions were not given to Commissioners if the charges or grounds for the Wells notice had changed. Even if a recommendation has changed, the Commissioners may well benefit from the additional background from the potential respondent's or defendant's side.

The Wells process usually occurs at the end of an investigation, but it generally should not be the only opportunity for enforcement staff and potential respondents or defendants to discuss the direction of an investigation. Early engagement where, for example, a potential respondent or defendant believes the staff is operating under a mistaken view of the facts could save both sides time and resources.

Similarly, the staff and the defendant might agree to a "white paper" process to address concerns about factual or legal issues in an investigation, particularly in cases where a potential respondent or defendant feels obligated to make a public disclosure of a Wells notice or to save on the costs of making a Wells submission. Like written Wells submissions, such white papers are provided to the Commission for their review and consideration.

A fair and transparent Wells process, as I have described, helps the Commission to fully understand both the positions of the staff in making an enforcement recommendation and those of the individual or entity that would be charged. This balanced approach serves the interest of justice and strengthens the integrity of our enforcement program.

The Wells process is the product of careful thought. Over fifty years ago, Chairman Bill Casey showed much foresight in asking Jack Wells, a New York attorney, to work with two former SEC Chairmen to make suggestions to improve the due process practices at the SEC. The Commission adopted many of their suggestions. The markets and jurisprudence have changed over that half-century. New Supreme Court and other courts' decisions have altered the landscape. We must take stock of the successes and the challenges that our enforcement program faces. The Wells procedures have proven their value over the years and even have been adopted by other regulatory agencies, such as the CFTC, although sometimes perhaps more in form than in substance. Eighteen years ago, on this platform, I raised the need for a revisiting and refreshing of the Wells process. The Commission has not yet done so. It is incumbent on us to rectify that.

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In much the same spirit, I recently revisited another process that implicates fairness and transparency: the simultaneous consideration of settlement offers and related requests for waivers from collateral consequences resulting from enforcement actions. It was previously the agency's practice to consider enforcement settlements and any related waiver requests in tandem. In recent years, however, the agency abandoned this practice. Enforcement staff negotiated settlements in one silo, the policy division considered waiver requests in another, and often on different timetables. The result was uncertainty for settling parties and inefficiency for the Commission and its staff.

My new statement makes clear that staff from the Enforcement Division and policy Divisions will present an offer of settlement in an enforcement action with a contemporaneous waiver request to the Commission for simultaneous consideration, unless the Commission determines that it wishes to consider them independently. This simultaneous approach will enable the Commission to consider both the proposed settlement and waiver request together—within the context of the relevant facts, conduct, and consequences, and with the benefit of the analysis

and advice of the Enforcement Division and the relevant policy Divisions—to assess whether the proposed resolution of the matter in its entirety achieves the agency's three-part mission. This approach will also avoid the pitfalls of fragmented review at different times, which is critical in reaching comprehensive settlements that are in the best interests of investors.

Of course, simultaneous consideration of a settlement offer and waiver request does not bind the Commission to accept the settlement offer. But this process is not meant to foreclose a settling entity from assessing its options when the Commission accepts its settlement offer, yet declines to approve its waiver request. Where this occurs, my expectation is that the staff will promptly notify the prospective respondent or defendant, who then must promptly notify the staff whether it agrees to move forward with that portion of the settlement offer accepted by the Commission. If the prospective respondent or defendant declines to move forward or otherwise withdraws its offer of settlement, the staff may re-evaluate the negotiated settlement terms, and a litigated proceeding may follow.

I consider this reform as a close cousin to the Wells process. Both aim to ensure that when the Commission exercises its enforcement authority, it does so fairly, transparently, and with the procedural rigor that engenders confidence in our work.

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But we are not finished with our work. To ensure that our enforcement staff can continue to serve the essential enforcement functions of the Commission, we must continue to examine, refine, and improve upon our Commission and enforcement processes.

More than half a century has passed since the formation of the committee that led to the Wells process as we know it today. As I said at the outset of my remarks, we are now in a different era. Markets have evolved, technologies have changed, and our enforcement program has grown and become more complex. And so again, I ask the question at the heart of our mission: how can we enforce the federal securities laws with fairness and transparency?

The answer, I submit, is that we should strive for enforcement processes that respect the rule of law, provide predictability, and protect the rights and interests of those with whom we interact. These processes should ensure that we act efficiently to conduct investigations and determine whether to recommend enforcement actions or close matters without delay or unnecessary publicity. And they should ensure that we seek to impose penalties and other relief that are appropriately tailored to the misconduct at issue, within statutory limitations and without adding further to shareholder injury.

Likewise, we should strive for enforcement processes that promote transparency. Those processes should ensure that we follow the Commission's public guidance, including on penalties and co-operation. Commission orders should provide the public with enough

information to understand why conduct violated the federal securities laws, and why particular relief was imposed. Practices for issuing termination and closing letters should sufficiently permit potential respondents or defendants, as well as recipients of document requests and subpoenas, to understand an investigation has concluded. We should clearly explain the procedures by which individuals who are subject to associational and penny stock bars (which are intended to be protective, rather than punitive, measures) can seek reinstatement, and the standards that the Commission will apply in assessing their applications.

The processes should ensure that we achieve consistent results, regardless of which office or unit conducts an investigation or litigates an enforcement action. Our processes should ensure that we avoid information silos and fragmented thinking, and that the work of the Enforcement Division (as well as that of the Examination Division) reflects the regulatory and policy objectives of the Commission, including the policy Divisions.

Finally, to faithfully steward the resources and responsibility that the public has entrusted to us, the Commission will set priorities for the Enforcement staff. We also need to make certain that we have the right incentive structure in place for our enforcement staff as they carry out their work to protect investors and safeguard our markets. If we reward the staff only for bringing enforcement actions, then we have discouraged the staff from determining not to recommend an enforcement action. A basic tenet of management is, "You get what you measure." The wrong incentives make it more difficult for the staff to follow the evidence and the law wherever it leads and instead encourage the staff to stretch the boundaries of existing law. Our goal is to reward the staff for their quality work and judgement on cases to bring, violations to charge, and relief to seek. All of this aligns with the belief that I share with Al Sommer: that the manner in which we achieve outcomes is critical.

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Finally, the challenges that we face today are different in form but not necessarily in substance from those that Al and his contemporaries encountered decades ago at the Commission. Finance today is surely faster, more global, more interconnected. But the fundamental dynamics remain: issuers seek capital, investors seek returns, and bad actors seek to defraud the public for personal gain. Eighteen years ago, I described the Wells process as one of the Commission's great procedural innovations to fulfill its mission of protecting investors; maintaining fair, orderly, and efficient markets; and facilitating capital formation.

Tonight, I reaffirm that conviction. The Wells process remains a critical due process mechanism that promotes fairness and transparency in the SEC's enforcement program. That mechanism is not an impediment to effective enforcement, but rather, a precondition for it, for processes perceived as unfair or opaque breed resistance and a lack of trust, making the critical work of

our enforcement staff more difficult and less effective. Conversely, when the public perceives our processes as fair and transparent, and when it is clear that the Commission and its staff review every case thoughtfully—with the benefit of all relevant context and perspectives—we sustain trust in the Commission and the markets that we oversee. The SEC will find and strike this balance in the years to come.

For now, I am grateful once again for the chance to continue this conversation in the spirit and memory of Al Sommer. It has been a pleasure speaking with you this evening. I welcome your active involvement in the issues I discussed tonight. And as we mark this twenty-fifth anniversary of the Sommer Lecture, I can think of no better wish than that the dialogue it inspires should continue for the next quarter century and beyond.

Thank you very much for your attention tonight.

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