

# A trending question: Litigate or settle?

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## SEC: Enforcement

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## Carl Ayers

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“The landscape is changing,” said **Andrew Calamari**, a partner with **Finn Dixon & Herling** in Stamford, Conn., and a former director of the SEC’s New York Regional Office. He spoke Jan. 10<sup>th</sup> during a **Sidley and SEC Historical Society** webinar examining a trend toward more defendants choosing to litigate against the SEC.



“Most SEC enforcement actions settle,” noted **Barry Rashkover**, partner with Sidley in New York, another SEC alum. “There are a lot of incentives” to do so, e.g., to avoid the high costs of protracted litigation and sidestep the wrath of Wall Street, he added.

## **Taking on your regulator comes with a cost**

“If you go to war with the SEC, you may win the case but your stock is going to drop like a stone,” Rashkover said. Big public companies “don’t want these consequences.”

Still, two decades ago it was rare for a defendant to joist in federal court with the SEC. Not so much today, he said. Others have predicted that more defendants will elect to contest SEC enforcement actions in court (*RCW*, Jan. 5, 2023).

Some defendants “feel they have no choice but to litigate because they feel it’s the only vindication they could get,” said **Silvia Serpe**, founding partner, **Serpe LLC** in New York.

A driving factor is the SEC, under Chairman **Gary Gensler**, “has become far more aggressive. I mean literally on a day-to-day basis,” she continued. It used to be she could call an SEC staff attorney, strike up a rapport and talk about a more favorable outcome for a client. That’s changed.

“The staff attorneys are feeling the pressure” from SEC headquarters in Washington to be more aggressive, Serpe said.

### **Green light on litigating**

That view found confirmation from the SEC employee on the panel, who stressed she was speaking for herself only and not the Commission. “The message is clear we shouldn’t be afraid to litigate,” said **Ladan Stewart**, regional trial counsel in the SEC’s new Crypto Assets and Cyber Unit.

The Commission strives to make more money available for litigation, too, she added. “What the Enforcement Division is recommending and what the Commission is authorizing are [U.S.] District Court actions and not contested” administrative proceedings, added Stewart.

“At the current time the message is pretty clear that we are aggressively litigating our cases,” she continued.

One reason for this is the Commission’s other avenue for bringing enforcement actions—internally through its administrative law setting—suffers from legal uncertainty given some successful and pending legal challenges.

The first strike came in the **U.S. Supreme Court**’s case five years ago upholding an investment adviser’s claims that the SEC ALJ setting was unconstitutional (*RCW*, June 22, 2018), recounted Rashkover. He also raised the current case before the SCOTUS—a decision should come by July—that also questions the constitutionality of the ALJ setting (*RCW*, Nov. 10, 2022).

### **Painful penalties**

Other factors feeding the urge to fight are “devastating” penalties, including hundreds of millions of dollars in settlements for “essentially a books and records violation,” said Calamari (*RCW*, Sept. 29, 2022).

Some companies and individuals feel they have no option because a loss in court would doom their livelihood anyway. A threat for hedge fund advisers comes in an enforcement action vacating their Reg D ability to raise money, noted Rashkover. While the SEC often issues administrative waivers to allow convicted advisers to continue to use Reg D, “there are no guarantees,” he said. “You could end up settling your case and not getting your waiver” because an enforcement action and the subsequent waiver process operate on two different tracks within the Commission, according to Rashkover.

### **Resolution times**

A panel of lawyers discussing litigation may present an inherent bias. A study three years ago found that it takes 10 days to resolve the average administrative proceeding but 27 times that to wrap up a federal court case.

Another advantage of the ALJ setting is you can get the SEC's entire case file within one week of an action being filed, said Serpe.

Normally, at the Wells Notice stage (when the Commission alerts a firm legal action is imminent), the defendant will request the SEC case file, said Calamari (RCW, Oct. 4, 2021). It's often up to the staff attorney. Some turn files over and others don't, although you'd get them eventually via discovery.

While you don't get the SEC case file right away in a court case, unlike with the ALJ, you can get the list of all names who can support the SEC's claims and perhaps a chart of all documents used by the Commission, said **Haima Marlier**, a partner with **Morrison Foerster** in New York. Her past also includes time at the SEC's New York Regional Office. Armed with this information, "you can quickly see who they've been talking to," she added.

An advantage of litigating is you can get discovery to help clients "understand why a resolution might be in their best interests," Marlier continued. You can also take depositions and then go back to the SEC with a stronger position—or a weaker one—to seek a settlement.

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