CORNERSTONE RESEARCH

Economic and Financial Consulting and Expert Testimony

SEC Enforcement Activity: Public Companies and Subsidiaries

Midyear FY 2018 Update

ANALYSIS AND TRENDS

Filings

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NYU Pollack Center for Law & Business

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Executive Summary

The SEC filed 15 new enforcement actions against public companies and their subsidiaries in the first half of FY 2018, the lowest semiannual total since the first half of FY 2013. This report highlights findings based on the Securities Enforcement Empirical Database (SEED), a collaboration between the NYU Pollack Center for Law & Business and Cornerstone Research.

The SEC enforcement actions discussed in this report only include actions against public companies and subsidiaries. As of March 2018, SEED also includes data on the individuals who are named defendants in these actions.[1] See page 3 for additional details.

Filings

- The recent trend of significantly lower SEC enforcement activity against public companies and their subsidiaries continued through the first half of FY 2018. (page 2)
- New actions against public companies and subsidiaries in the first half of FY 2018 declined almost 70 percent from the first half of FY 2017. (page 2)

New Analysis: Individuals

- The majority (67 percent) of public company and subsidiary actions in 1H FY 2018 did not have an associated individual defendant. (page 3)
- Of the five new actions with individual defendants in 1H FY 2018, four involved Issuer Reporting and Disclosure allegations. (page 3)

Allegations

- Two public company and subsidiary actions in 1H FY 2018 included allegations of steering investors to higher fee share classes of mutual funds. (page 4)
- The two public company and subsidiary actions in 1H FY 2018 with FCPA allegations already match the total number of actions in the last eight months of FY 2017. (page 4)

Industry

- The Finance, Insurance, and Real Estate industry accounted for almost 70 percent of all new public company and subsidiary actions in 1H FY 2018. (page 5)

The SEC's low rate of new actions against public company and subsidiary defendants continued into the first half of FY 2018, accompanied by a narrow range of industries targeted in these actions.

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Timing of Resolutions

- In the first half of FY 2018, 87 percent of public company and subsidiary actions were resolved on the same day they were initiated. (page 6)

Cooperation

- More than half of public company and subsidiary defendants cooperated with the SEC in 1H FY 2018. (page 7)

Monetary Settlements

- Monetary settlements in public company and subsidiary actions declined to $65 million in 1H FY 2018, the lowest semiannual total in the Research Sample. (page 8)
- The largest monetary settlement imposed on an individual in 1H FY 2018 was $0.2 million. (page 9)
- The largest monetary settlement for any single defendant in 1H FY 2018 was $13 million imposed on a subsidiary defendant. (page 9)

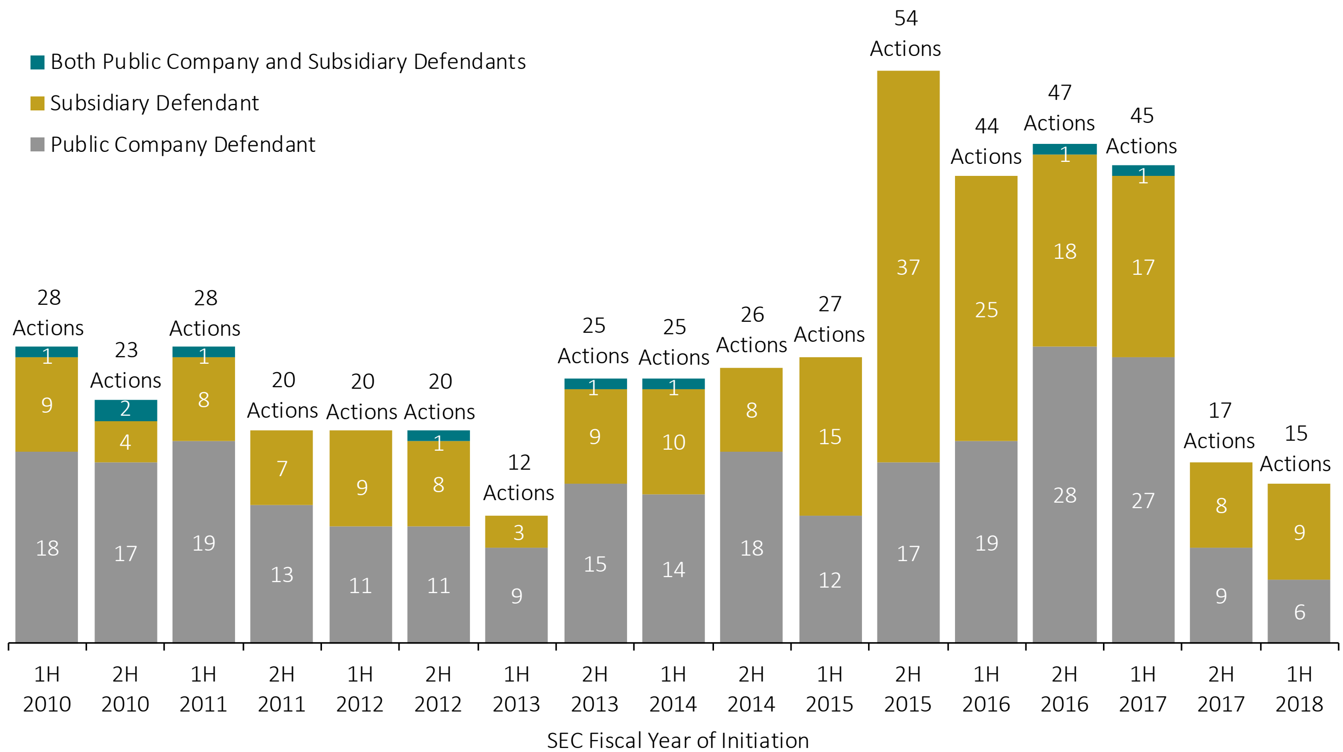
Number of Filings

- The SEC filed 15 new enforcement actions against public companies and their subsidiaries in the first half of FY 2018, a 67 percent decline from 45 in the first half of FY 2017.
- The FY 2010–FY 2017 average is approximately 29 actions per half year and the median is approximately 26 actions per half year.
- The majority (60 percent) of the 15 new actions against public companies and subsidiaries in 1H FY 2018 had a subsidiary as a defendant, compared to the FY 2010–FY 2017 semiannual average of 40 percent.

The trend of significantly lower enforcement actions filed against public companies and subsidiaries continued from the second half of FY 2017.

- Administrative proceedings accounted for 80 percent of new actions against public companies and subsidiaries in 1H FY 2018, the lowest percentage since 1H FY 2014.

Figure 1: Public Company and Subsidiary SEC Actions
FY 2010–1H FY 2018



Source: Securities Enforcement Empirical Database (SEED)
Note: Relief defendants are not considered.

New Analysis: Filings Involving Individuals

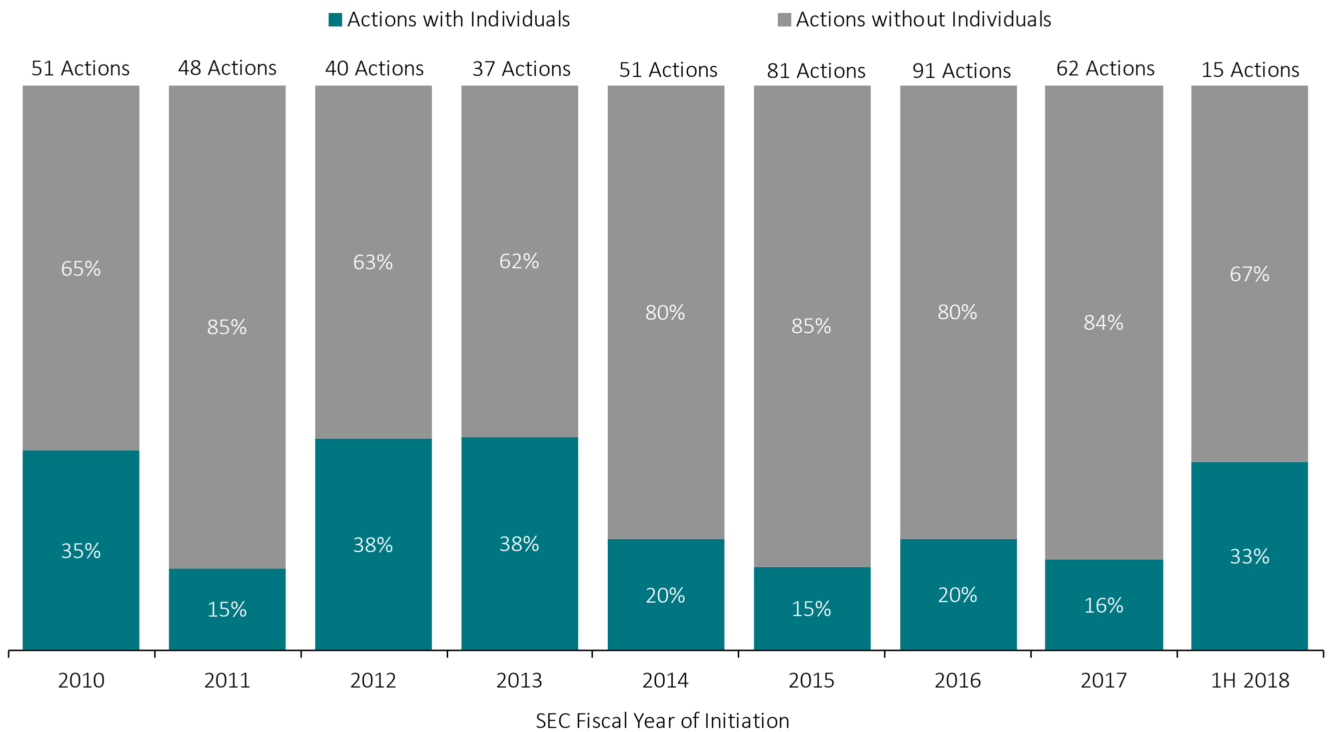
SEED includes actions against public companies and their subsidiaries. As of March 2018, SEED also includes information on individuals named as defendants in these actions[2]—referred to in this report as "individual defendants." (See Research Sample)

- Ten of the 15 public company and subsidiary actions in 1H FY 2018 (67 percent) did not have any individual defendants. The FY 2010–FY 2017 average is 76 percent.
- The five public company and subsidiary actions in 1H FY 2018 involving individual defendants had an average of 2.4 individuals per action, or 12 total.

SEED now includes information on individuals who are named defendants in public company and subsidiary actions.

- Nine of the 12 individual defendants associated with the five public company and subsidiary actions held positions as CEO, CFO, or Controller.
- Of the five public company and subsidiary actions with individual defendants in 1H FY 2018, four involved Issuer Reporting and Disclosure allegations.

Figure 2: Breakdown of Public Company and Subsidiary Actions with Individual Defendants
FY 2010–1H FY 2018



Source: Securities Enforcement Empirical Database (SEED)

Note: Relief defendants are not considered. Actions involving individuals include actions with public company or subsidiary defendants and at least one individual defendant. Percentages may not add to 100 percent due to rounding.

Classification of Allegations

- Issuer Reporting and Disclosure and Investment Advisor/Investment Companies were the most common allegation types in actions against public company and subsidiary defendants in the first half of FY 2018.

The increased concentration of Broker Dealer and Investment Advisor/Investment Companies actions in 1H FY 2018 (compared to the FY 2010–FY 2017 average) followed the SEC's announced focus on the "main street investor."[3]

- The number of actions with FCPA allegations in 1H FY 2018 (two) matches the total for the last eight months of FY 2017, but is lower than the 1H FY 2010–2H FY 2017 semiannual average of almost 5.6 actions.
- Two of the 15 actions in 1H FY 2018 included claims of steering investors to higher fee share classes of mutual funds (both are Investment Advisor/Investment Companies actions). These actions are examples of the SEC's focus on retail investors under the Retail Strategy Task Force created in September 2017.[4]

Figure 3: Heat Map of Allegations against Public Company and Subsidiary Defendants
FY 2010–1H FY 2018

	SEC Fiscal Year of Initiation									
Allegation Type	Average 2010–2017	2010	2011	2012	2013	2014	2015	2016	2017	1H 2018
Issuer Reporting and Disclosure	37%	43%	33%	30%	49%	49%	23%	26%	39%	27%
Investment Advisor/ Investment Companies	11%	6%	4%	10%	14%	10%	6%	20%	21%	27%
Broker Dealer	10%	10%	13%	10%	0%	14%	12%	12%	13%	20%
Foreign Corrupt Practices Act	20%	24%	35%	25%	14%	14%	12%	20%	16%	13%
Securities Offering	7%	6%	4%	8%	19%	4%	1%	9%	5%	7%
Municipal Securities/ Public Pensions	10%	4%	10%	10%	0%	4%	40%	9%	0%	0%
Market Manipulation	2%	0%	0%	5%	5%	2%	0%	0%	0%	0%
Other	4%	8%	0%	3%	0%	4%	5%	4%	6%	7%
Number of Actions	58	51	48	40	37	51	81	91	62	15

Legend	0%	1–10%	11–20%	21–50%	51–100%

Source: Securities Enforcement Empirical Database (SEED)
Note: Relief defendants are not considered. Percentages may not add to 100 percent due to rounding. "Other" includes actions categorized by the SEC as "Other" or "Transfer Agent."

Industry

SEED classifies public company defendants and the parent company of subsidiary defendants by their Standard Industrial Classification (SIC) codes.

- In the first half of FY 2018, actions with public company and subsidiary defendants in the Finance, Insurance, and Real Estate industry accounted for 10 actions, or 67 percent of all actions. More than half of public company and subsidiary actions were filed against Finance, Insurance, and Real Estate defendants in four of the prior six fiscal years.
- Half of the 1H FY 2018 actions against Finance, Insurance, and Real Estate defendants targeted Commercial Banks (five actions), consistent with the trend over the prior three fiscal years.
- The only other industries targeted in 1H FY 2018 in public company and subsidiary actions were Manufacturing (three actions) and Mining (two actions).
- The two public company and subsidiary actions against Mining defendants targeted a Gold and Silver Ores mining company and a Metal Mining Services firm, neither of which had been targeted in any public company or subsidiary actions in the prior eight fiscal years.

All public company and subsidiary defendants were in the Finance, Insurance, and Real Estate; Manufacturing; or Mining industries.

Figure 4: Heat Map of Industries of Public Company and Subsidiary Defendants
FY 2010–1H FY 2018

SIC Industry Division	SEC Fiscal Year of Initiation									
	Average 2010–2017	2010	2011	2012	2013	2014	2015	2016	2017	1H 2018
Finance, Insurance, and Real Estate	48%	35%	33%	53%	46%	53%	63%	58%	42%	67%
Manufacturing	28%	37%	38%	33%	27%	20%	17%	19%	32%	20%
Services	10%	22%	15%	8%	5%	12%	9%	3%	8%	0%
Mining	4%	2%	8%	0%	8%	4%	4%	3%	5%	13%
Other	10%	4%	6%	8%	14%	12%	7%	16%	13%	0%
Number of Actions	58	51	48	40	37	51	81	91	62	15

Source: Securities Enforcement Empirical Database (SEED)

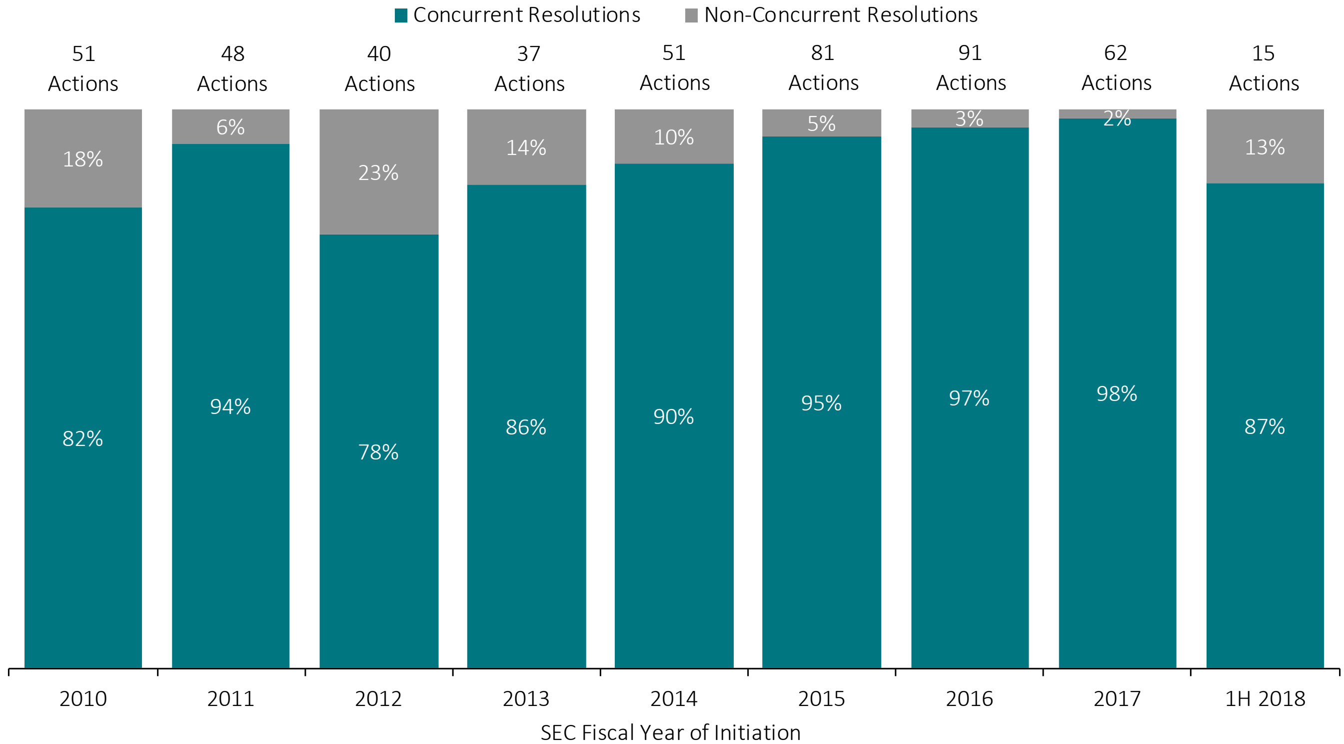
Note: Relief defendants are not considered. SIC industry divisions are as of the SEC enforcement action initiation date, or otherwise are as of the latest available date within the five-year period preceding the initiation. Subsidiary defendants are categorized according to the SIC industry division of their public parent company. “Other” contains all SIC industry divisions that were not in the top four by average action count over fiscal years 2010 to 2017. Percentages may not add to 100 percent due to rounding.

Timing of Resolutions

- In the first half of FY 2018, 13 public company and subsidiary actions (87 percent) were resolved on the same day they were initiated (concurrent resolutions).[5] The FY 2010–FY 2017 average is 90 percent.
- Both non-concurrent actions in 1H FY 2018 were federal court actions involving Issuer Reporting and Disclosure allegations.
- There are five unresolved actions initiated since FY 2010 against public company and subsidiary defendants (all civil actions). Of these, one was initiated in the first half of FY 2018 and the longest running was initiated in FY 2012.

The two litigated actions resolved at trial since FY 2010 involved Issuer Reporting and Disclosure allegations.

Figure 5: Timing of Resolutions for Actions with Public Company and Subsidiary Defendants
FY 2010–1H FY 2018



Source: Securities Enforcement Empirical Database (SEED)

Note: Only public company and subsidiary defendants are considered when determining whether an action resolved concurrently (i.e., if a public company defendant resolved concurrently but an individual defendant in the same action did not, the action would be classified in the analysis as having a concurrent resolution). Relief defendants, individual defendants, and non-public company/non-subsidiary defendants are not considered. Actions that are initiated and resolved on the same day are concurrent resolutions. Percentages may not add to 100 percent due to rounding.

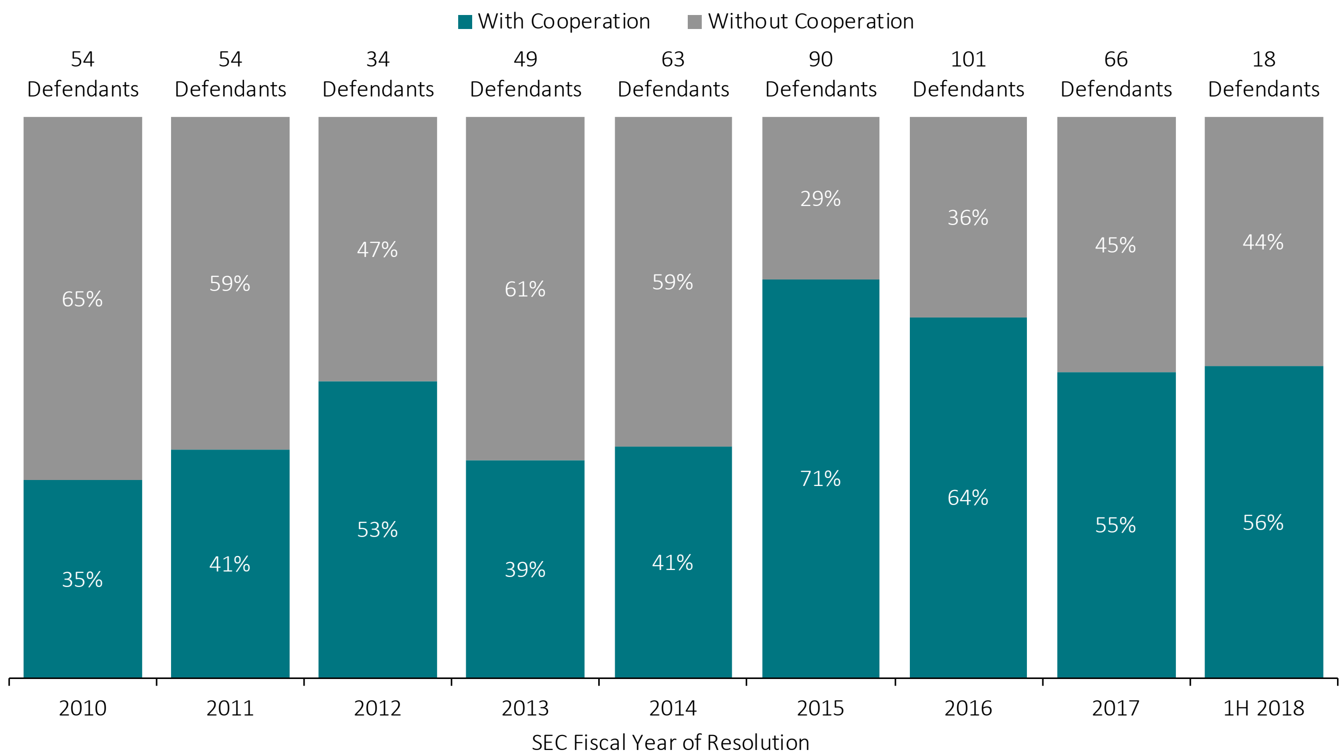
Cooperation Noted in Settlements

The SEC considers four factors when negotiating a settlement with a cooperating defendant: “self-policing, self-reporting, remediation, and cooperation.”[6] SEED measures the latter three factors as an indication of whether a public company or subsidiary defendant cooperated with the SEC based on whether the SEC acknowledges voluntary reporting or explicitly mentions “remediation” or “cooperation” by the defendant in the settlement announcement (collectively referred to in this report as “cooperation” or “cooperated”).

- In the first half of FY 2018, 56 percent of public company and subsidiary defendants in public company and subsidiary actions cooperated with the SEC, compared to the FY 2010–FY 2017 average of 50 percent.
- Of the 10 public company and subsidiary defendants that cooperated in 1H FY 2018, three were involved in Broker Dealer actions.

More than half of public company and subsidiary defendants in public company and subsidiary actions cooperated in 1H FY 2018, compared to less than a third in 2H FY 2017.

Figure 6: Cooperation Noted in Settlements with Public Company and Subsidiary Defendants
FY 2010–1H FY 2018



Source: Securities Enforcement Empirical Database (SEED)

Note: Relief defendants, individual defendants, and non-public company/non-subsidiary defendants are not considered. Actions resolved through trial are excluded. An action with cooperation indicates a public company or subsidiary defendant’s cooperation with the SEC prior to the non-trial resolution of that action. The words “cooperation” or “remediation” must be mentioned in the document detailing the non-trial resolution, or the SEC must acknowledge voluntary reporting by the defendant. Settlements are counted at the defendant level.

Monetary Settlements

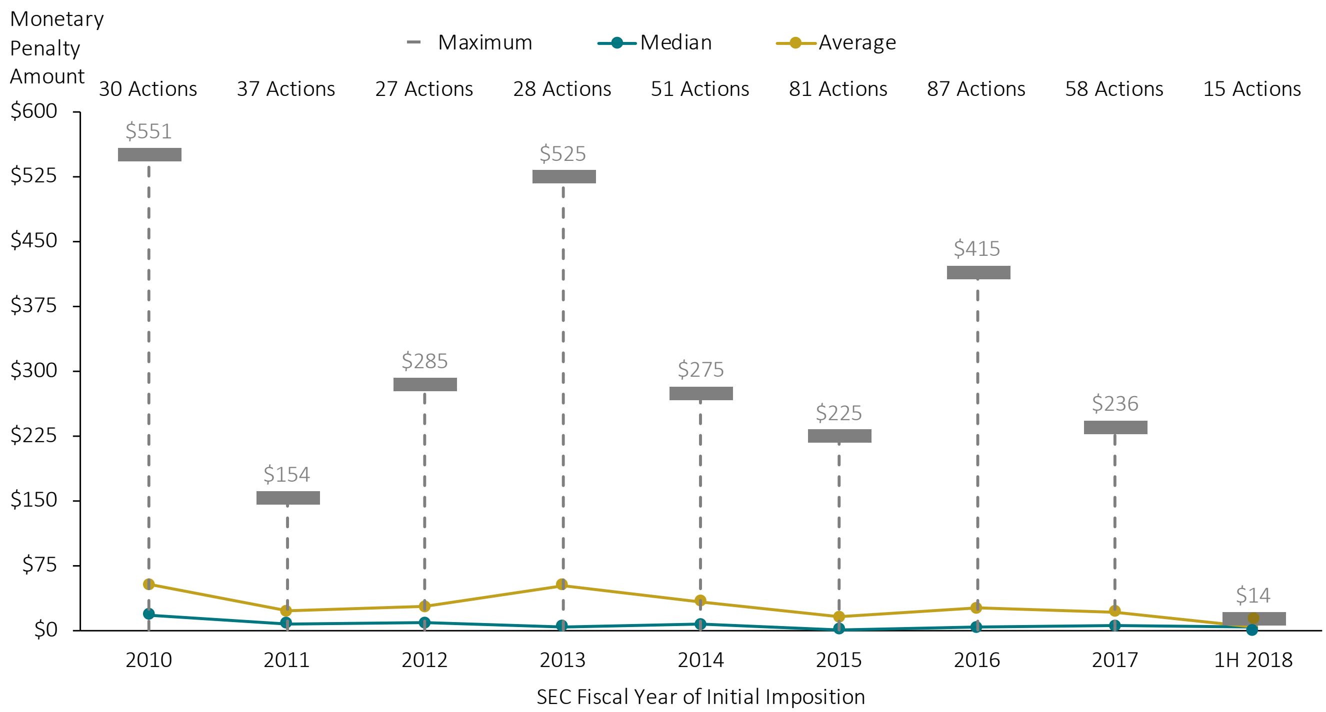
SEED includes data for monetary settlements imposed on all defendants in public company and subsidiary actions: parent, subsidiary, individual, and other defendants.[7]

- In the first half of FY 2018, monetary settlements decreased substantially from prior fiscal years. The maximum monetary settlement of $14 million was by far the lowest maximum monetary settlement in any half year in the database.
- Similarly, the average monetary settlement in 1H FY 2018 was $4.3 million, significantly below the next-lowest semiannual average of $13.3 million in 2H FY 2015.
- In 1H FY 2018, 54 percent of the total monetary settlements imposed involved actions with Broker Dealer or Investment Advisor/Investment Companies allegations.
- The majority of monetary settlements in public company and subsidiary actions are imposed on public company and subsidiary defendants, not individual defendants.

Monetary settlements declined significantly.

Figure 7: Monetary Settlements Imposed on All Defendants in Public Company and Subsidiary Actions
FY 2010–1H FY 2018

(Dollars in Millions)



Source: Securities Enforcement Empirical Database (SEED)

Note: Relief defendants are not considered. For actions where monetary settlements are not imposed on all defendants in the same fiscal year, actions are classified by the first fiscal year in which a monetary settlement was imposed. There are several actions for which not all defendants have settled. Total monetary settlements for those actions only include monetary settlements through March 31, 2018.

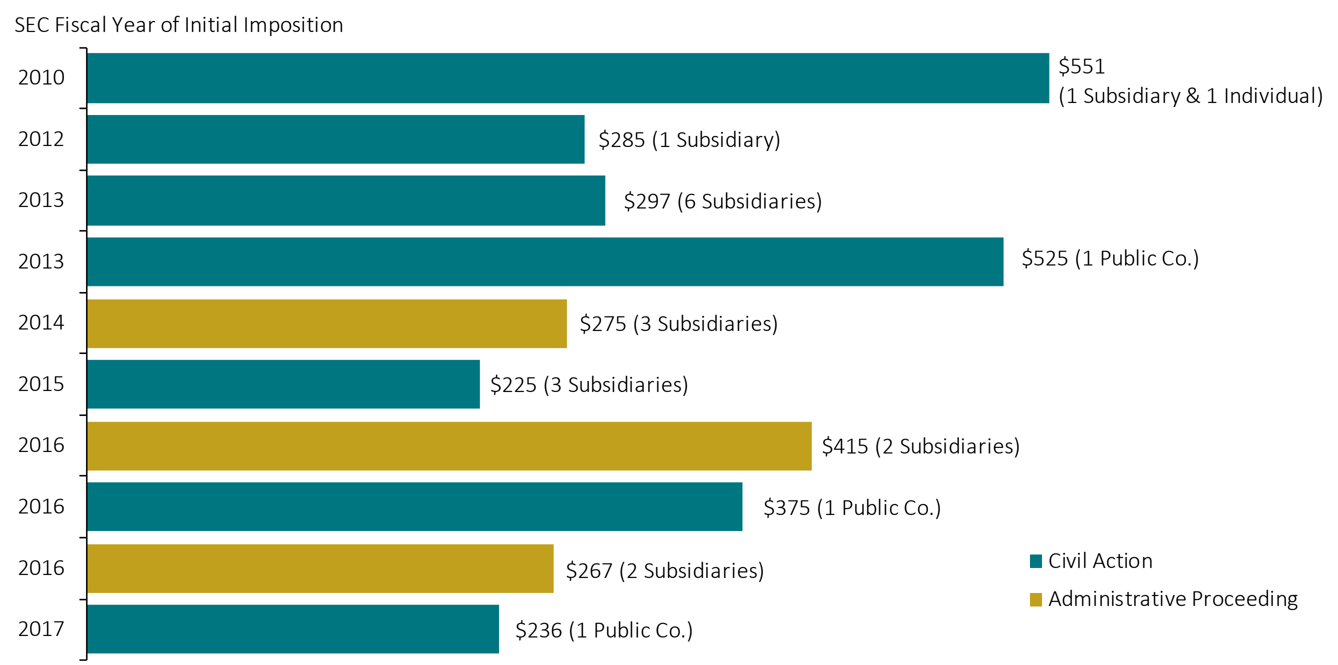
The top 10 monetary settlements imposed in public company and subsidiary actions reflect the total monetary settlement imposed in the action on all defendants (including individuals), instead of only the monetary settlements imposed on public companies and subsidiaries.

- Only one action in the top 10 monetary settlements imposed in public company and subsidiary actions included a monetary settlement with an individual defendant. That settlement accounted for $1 million of the $551 million total.
- In 1H FY 2018, there were no actions with monetary settlements large enough to be included in the top 10 monetary settlements imposed in public company and subsidiary actions from FY 2010 through 1H FY 2018.
- The largest monetary settlement in public company and subsidiary actions imposed on an individual in 1H FY 2018 was $0.2 million. The largest settlement imposed on any single defendant was $13 million, imposed on a subsidiary defendant.

The largest monetary settlement for a public company or subsidiary action in 1H FY 2018 was $14 million and was imposed on three subsidiary defendants.

Figure 8: Top 10 Monetary Settlements Imposed in Public Company and Subsidiary Actions
FY 2010–1H FY 2018

(Dollars in Millions)



Source: Securities Enforcement Empirical Database (SEED)

Note: There were no monetary settlements in FY 2011 or 1H FY 2018 that were large enough to be included in the top 10. Relief defendants are not considered. For actions where monetary settlements are not imposed on all defendants in the same fiscal year, actions are classified by the first fiscal year in which a monetary settlement was imposed. There are several actions for which not all defendants have settled. Total monetary settlements for those actions only include monetary settlements through March 31, 2018.

Research Sample

- The Securities Enforcement Empirical Database (SEED), a collaboration between the NYU Pollack Center for Law & Business and Cornerstone Research, identifies 476 SEC enforcement actions initiated against 428 public company defendants and their subsidiaries between October 1, 2009, and March 31, 2018 (http://seed.law.nyu.edu).
- SEED identifies 225 individuals that are named defendants in the 476 actions initiated against public company defendants and their subsidiaries between October 1, 2009, and March 31, 2018 (http://seed.law.nyu.edu).
- The sample used for the majority of this report is referred to as "enforcement actions initiated against public company and subsidiary defendants" and includes only those enforcement actions with public companies or their subsidiaries listed explicitly as defendants. The sample does not include cases where the allegations relate exclusively to delinquent filings.
- Public companies are defined as those that traded on a major U.S. exchange as identified by the Center for Research in Security Prices (CRSP) at the time the enforcement action was initiated, or otherwise within the five-year period preceding the initiation. Thus, public companies that traded over-the-counter or only on major non-U.S. exchanges are excluded, as are companies that did not become publicly traded until after the enforcement action was initiated.

SEED provides easily searchable and verified data on SEC enforcement actions to researchers, counsel, and corporations.

- Subsidiaries are defined as those entities that had a publicly traded parent company at the time the enforcement action was initiated or otherwise within the five-year period preceding the initiation. The public parent companies of subsidiaries were identified as those cited in the enforcement action document initiating proceedings when available, or those identified through SEC filings if no parent company was mentioned in the initial enforcement action document.
- Individuals are defined as individuals who are named defendants in actions against public companies or their subsidiaries

Endnotes

[1] SEC fiscal years begin on October 1 of the prior year and end on September 30. SEC fiscal year 2010 through the first half of fiscal year 2018 spans October 1, 2009, to March 31, 2018.

[2] Information is included on individuals that are defendants in SEC actions with a public company or subsidiary defendant for all actions filed beginning FY 2010.

[3] See, e.g., U.S. Securities and Exchange Commission, "Division of Enforcement Annual Report: A Look Back at Fiscal Year 2017," https://www.sec.gov/files/enforcement-annual-report-2017.pdf.

[4] "SEC Announces Enforcement Initiatives to Combat Cyber-Based Threats and Protect Retail Investors," SEC Press Release 2017-176, September 25, 2017, https://www.sec.gov/news/press-release/2017-176; "The SEC Enforcement Division's Initiatives Regarding Retail Investor Protection and Cybersecurity," Stephanie Avakian, Co-Director, Division of Enforcement, U.S. Securities and Exchange Commission, October 26, 2017, https://www.sec.gov/news/speech/speech-avakian-2017-10-26.

[5] This analysis only considers the resolutions of public companies and subsidiaries and uses the date the first resolution was announced to measure whether the resolution was concurrent or non-concurrent. There may be instances where the analysis states the resolution was concurrent, but the first announced resolution did not have the same terms as the final resolution.

[6] "The SEC's Cooperation Program: Reflections on Five Years of Experience," Andrew Ceresney, Director, Division of Enforcement, U.S. Securities and Exchange Commission, May 13, 2015, https://www.sec.gov/news/speech/sec-cooperation-program.html.

[7] Total monetary settlements include disgorgement, prejudgment interest, civil penalties, and other monetary penalties imposed in public company and subsidiary actions. For actions where monetary settlements are not imposed on all defendants in the same fiscal year, actions are classified by the first fiscal year in which a monetary settlement was imposed. There are five actions for which not all defendants have settled—total monetary settlements for those actions only include monetary settlements through March 31, 2018.

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The authors request that you reference the NYU Pollack Center for Law & Business and Cornerstone Research in any reprint of the information or figures included in this report.

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