PROGRAM MATERIALS
Program #1893
November 19, 2008

# The New SEC Enforcement Manual: The Key Points and their Impacts on Current Practice



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**THE NEW SEC ENFORCEMENT MANUAL:**
**THE KEY POINTS AND THEIR IMPACT ON PRACTICE**
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**Washington, D.C.**
**November 19, 2008**

## I. Introduction

A. On October 6, 2008, the SEC's Division of Enforcement issued its *Enforcement Manual.*

1. This is the first compilation of Enforcement Division procedures made available to the public.

2. Previously, the Division had internal procedures and practices, some of which were recorded in the so-called "red book," which has not been made public.

B. There have been repeated requests for the Division to issue a procedures manual over the years. For example:

1. The minority report of the Senate committee inquiring into the botched Pequot Capital inquiry called for the Division to formalize its procedures to add structure and transparency. Minority Staff of S. Comm. On Finance, 110th Cong. 1st Sess., "The Firing of an SEC Attorney and the Investigation of Pequot Capital Management at 46 (S. Prt. 110-28 Aug. 2007).

2. Former SEC Commissioner Atkins has called for the Division to formalize its procedures. *See, e.g.,* Commissioner Paul S. Atkins, SEC, "Remarks to the SEC Speaks in 2008 Program of the Practicing Law Institute" (Feb. 8, 2008).

3. The Department of Justice procedures have long been available as an aid to practitioners in the *U.S. Attorney's Manual.*

C. Significant portions of the *Manual* focus on internal procedures used by the Division. A number of sections direct the staff to follow certain procedures in conducting an investigation. Key areas which will be discussed here include:

1. Overview: purpose of the *Manual* and its general content;

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2. The Wells process;

3. Cooperation and privilege;

4. Parallel proceedings;

5. Documents and testimony; and

6. Conclusions.

## II. Overview: The Purpose of the *Manual*

A. Purpose: The purpose and scope of the *Manual* is defined in Section 1.1 which states in part:

> The Enforcement Manual . . . is an electronic document designed to be a reference for the . . . [SEC Enforcement staff] in investigations . . . It contains various general policies and procedures and is intended to provide guidance only to the staff of the Division. It is not intended to, and does not, and may not be relied upon to create any rights, substantive or procedural, enforceable at law by any party in any matter civil or criminal.

B. Preparation: The *Manual* was prepared under the supervision of the Office of Chief Counsel, Division of Enforcement. That office consulted with a number of other staff divisions.

C. Mission statement: According to the *Manual*, the mission statement of the Division is to "protect investors and the markets by investigating potential violations of the federal securities laws and litigating the SEC's enforcement actions."

D. The *Manual* is divided into five key sections:

1. Introduction;

2. A guide to matters under inquiry and the stages of informal and formal investigations;

3. A guide to investigative practices;

4. Privileges and protections; and

5. Cooperation with other agencies and organizations.

E. Updates: The staff intends to periodically update the *Manual.*

F. Use for practitioners

1. While the *Manual* specifies that it is for internal use only and does not create rights in third parties, practitioners in this area would be well served by studying the entire *Manual* to familiarize themselves with the internal workings of the Division of Enforcement.

2. The limitations on the use of the *Manual* are consistent with those of the *U.S. Attorney's Manual*

## III. The Wells Process

A. Overview: In the narrow sense, the process refers to the Wells Notice. That notice is given to those against whom the staff is considering recommending that an enforcement action be brought. In its broader and perhaps more fundamental sense, the Wells Process is the entire process by which enforcement recommendations are formulated, discussed with potential defendants and through which cases are frequently resolved. The process is largely governed by Release No. 5310 and Rule 5(c) of the SEC's Rules of Informal and Other Procedures. To some extent, it is also governed by custom and practice.

B. Section 2.4 of the *Manual* discusses the Wells Process.

1. The Section begins with a brief review of the origins of the Process.

   a. The process dates to June 1972 and an advisory committee chaired by then Commissioner John Wells. That committee issued a report which resulted in a significant alteration of the existing process.

   b. Previously, the staff was not permitted to initiate settlement discussions or negotiate the terms of an offer of settlement before the action had been authorized by the Commission. The staff was also "precluded from indicating to the prospective defendant or respondent the particular recommendations that the staff intends to make to the Commission."

2. The Wells committee recommended that the process be changed. It concluded that "We think that frank discussions between the staff and opposing counsel concerning the staff's conclusions and probable recommendation to the Commission would encourage settlements."

3. The policies adopted under Release 5310 and Rule 5(c) implemented the spirit of the Wells Committee report. Those policies, to a large extent, are reiterated in the *Manual.*

4. The initial subsection encourages the staff to provide a written notice to the potential defendant or respondent. That notice is to identify the specific charges, give the recipient an opportunity to provide a statement and set a reasonable time limit for the submission of that statement.

a. The staff has the discretion to reject a submission if the person making it limits its admissibility under Federal Rule of Evidence 408 regarding settlements or in some other manner that is inconsistent with its intended use under Release 1662. The staff also has the discretion to reject the submission if it exceeds the specified length.

b. These provisions reflect current staff practice.

c. While both Release 5310 and Rule 5 of the SEC's Informal and Other Procedures make it clear that the staff has discretion to give a Wells notice, if one is submitted the staff must transmit it: "any submissions by interested persons will be forwarded to the Commission in conjunction with the staff memorandum." 17 C.F.R. §205.5 (c). For this reason, some practitioners request during testimony that the staff furnish notice of any recommendation regarding a possible enforcement action.

5. The notice is to be provided when the investigation is "substantially complete as to the recipient . . ."

6. In certain instances, it may not be appropriate to provide a notice. These include when an immediate enforcement action is necessary to protect investors (for example, in cases where a TRO or a asset freeze may be necessary to stop an on-going fraud).

7. One key subsection is "The Post-Notice Wells Process." Here. the staff is afforded "discretion to allow the recipient of the notice [the opportunity] to review non-privileged portions of the investigative file, including documents that the recipient likely would receive during the discovery if the Commission were to file a recommended action or proceeding." In considering this request, the staff is directed to "keep in mind:"

   a. Whether access would be "a productive way" for the staff and the notice recipient to assess the strength of the evidence on which the staff recommendation is based;

   b. Whether the notice recipient invoked the Fifth Amendment or otherwise refused to testify during the investigation; and

   c. The stage of the proceeding and whether others have yet to testify.

8. The opportunity to review portions of the staff's evidence, is a significant advancement in enforcement procedures.

   a. Previously, the staff did not typically grant access to its evidence, although some offices and sections of enforcement experimented with the process in certain cases.

b. Former Commissioner Atkins had called for "open jacket" discovery as it is called in the criminal cases. Paul S. Atkins and Bradley J. Bondi, Evaluating the Mission: A Critical Review of the History and Evolution of the SEC Enforcement Program, 13 Fordham J. Corp. & Fin. L. 367 (2008); Commissioner Paul S. Atkins, SEC, "Remarks to the SEC Speaks in 2008 Program of the Practicing Law Institute" (Feb. 8, 2008).

C. The *Manual* does not discuss the impact of invoking the Fifth Amendment on the process, although it does list it as a consideration as to whether the staff should permit open jacket discovery during the Wells Process.

1. Section 4.1.3 discusses the Fifth Amendment "against self-incrimination." The Section notes that a witness has the right to invoke the Amendment and decline to testify. Typically, the staff will require testimony or an affidavit by a person invoking his or her Fifth Amendment rights.

a. A witness is not permitted to make a "blanket" assertion.

b. In some cases, it may be appropriate to permit the person invoking the privilege under the amendment to do so by affidavit. The circumstances are not defined.

c. In some instances, it may be necessary for the party asserting rights under the amendment to appear. The reasons include "obtaining a clear and specific privilege assertion on the records, allowing the staff to probe the assertion of the privilege assertion, and allowing the staff to determine whether there are grounds to challenge the assertion."

d. According to the *Manual*, during litigation, the SEC can assert that an adverse inference should be drawn against the asserting party.

2. The *Manual* does not state that asserting the Fifth Amendment will have any impact on the Wells Process. In practice however, it may have a significant impact.

a. While the *Manual* discusses the Amendment in terms of "self-incrimination," in fact that phrase does not appear in the text of the Amendment, which only provides that "no person shall be compelled on any criminal case to be a witness against himself."

b. A person asserting the Fifth Amendment in testimony is typically told that an adverse inference may be drawn, a point not mentioned in the *Manual. But see, Baxter v. Palmigiano*, 425 U.S. 308, 318 (1976) (adverse inference can be drawn in civil proceeding when person would be expected to defend) and *SEC v. O'Brien*, 467 U.S. 735 (1984) (the SEC's investigations do not have targets).

c. During the Wells Process, the staff will decline to discuss the case beyond identifying the barest of information about the proposed recommendation.

i. When the notice is furnished, the staff provides little information beyond the Sections violated and the relief sought;

ii. In post notice meetings, the staff will not discuss the case with the notice recipient. This seems some what inconsistent with the purpose of the notice. It also seems at odds with the fundamental purpose of the Fifth Amendment and the Commission's law enforcement function. *See, e.g., Ohio v. Reiner,* 532 U.S. 17, 21 (2001)("one of the Fifth Amendment's basic functions…is to protect innocent men . . . who otherwise might be ensnared by ambiguous circumstances"). *Berger v. U.S.,* 295 U.S. 78, 88 (1935) (government may strike hard blows, but they must be fair), *see also,* Section 3.3.2 noting that, unlike grand jury proceedings, Commission investigations do not have targets.

iii. The staff will also typically decline to permit the notice recipient to review any of the underlying evidence.

iv. Cooperation and privilege

## IV. Cooperation and Privilege

A. Background: Section 4.3, titled "Waiver of Privilege," discusses cooperation and credit for that cooperation in the charging process. The Commission's Report of Investigation Pursuant to §21(a) of the Securities Exchange Act of 1934 and Commission Statement on the Relationship of Cooperation to Agency Enforcement Decisions, SEC Rel. No. 34-44969 (Oct. 23, 2001) ("the *Seaboard* Release"), also discusses the question of cooperation credit. That Release notes that cooperation is keyed to the production of all of the facts. In some instances, that may require that a company not assert privilege. In return, the company may receive cooperation credit in the form of not being prosecuted or a reduced sanction. In the example in the *Seaboard* Release, drawn from the underlying enforcement investigation, the company was not prosecuted, based in part on its cooperation which included not asserting privilege.

B. No waiver requests: Section 4.3 directs the staff not to request a waiver. This is the first flat statement on this point. It mirrors the position recently articulated in the new chapter to the U.S. Attorney's Office Manual authored by Deputy Attorney General Filip. U.S. Department of Justice, Executive Office for U.S. Attorneys, United States Attorneys' Manual, tit. 9, ch. 28 (Aug. 28, 2008). *See*

*also,* Section 4.1.1 discussing the attorney client privilege; *cf* Thomas O. Gorman, New DOJ Cooperation Principles: Substituting the Culture of Avoidance for the Culture of Waiver, 22 Bloomberg Law R. 1 (Sept. 29, 2008).

C. The Section appears to define cooperation in two ways:

1. All facts: A party seeking cooperation credit "must disclose all such facts within the party's knowledge." Privilege waivers are not required, just all the facts.

2. Other information/acts: Another form of cooperation is "voluntary production of relevant factual information the staff did not directly request and otherwise might not have uncovered; requesting that corporate employees cooperate with the staff and making all reasonable efforts to secure such cooperation; making witnesses available for interviews when it might otherwise be difficult or impossible for the staff to interview the witnesses; and assessing in the interpretation of complex business records." These examples are drawn from, and consistent with the *Seaboard* Release.

D. The *Manual* provides that the waiver of privilege is not required to obtain cooperation credit: "A party's decision to assert a legitimate privilege will not negatively affect their claim to credit for cooperation. The appropriate inquiry in this regard is whether, notwithstanding a legitimate claims or privilege, the party has disclosed all relevant underlying facts within its knowledge."

1. This statement presumes that the underlying facts about the matter under inquiry are not privileged.

2. If however, the facts were gathered in an internal investigation conducted by independent counsel, much of that investigation will be privileged.

3. The *Manual* however takes the position that the underlying facts are not privileged. If this statement is correct, then all the facts can be produced without waiving privilege.[2] If however, those facts are privileged, then it would appear that under the *Manual* cooperation credit may not be earned when there is an assertion of privilege.

4. The *Manual's* position on the waiver of privilege appears to be inconsistent. For corporate internal investigations, Section 4.3 asserts that the underlying facts are not privileged. In contrast, Section 2.3.4 states that an Action Memo, which contains a fact section and an analysis section is privileged.

[2] This assumes that facts were not obtained under a joint defense agreement. If relevant facts were obtained under such an agreement it would appear that waiver would be required to produce all the facts. For this reason the recent revisions to DOJ's cooperation policies suggest that issuers may want to refrain from entering into joint defense agreements. *See* Section IV (B) *supra*.

5. Previously, the staff insisted that privilege need not be waived to earn cooperation credit. If however, the company wanted to maximize cooperation credit and have at least an opportunity to avoid being charged, the waiver was required according, to statements made by the staff. Linda Thomsen, Speech by SEC staff: Remarks Before the Mutual Fund Directors Forum 7th Annual Policy Conference (Apr. 12, 2007).

E. Confidentiality agreements, according to the *Manual*, offer another opportunity for an issuer to cooperate without waiving privilege.

1. These agreements, discussed in Section 4.3.1, permit a party to furnish privileged material to the staff. In return, the staff will agree that the production is not a waiver as to third parties.

2. The Section cautions that some courts do not accept this principle.

3. In fact, virtually every circuit court which has considered the question has rejected the notion that a party can produced privileged material without waiving privilege. *Permian Corp. v. United States*, 665 F.2d 1214, 1216-17 (D.C. Cir. 1981) (the court held that the company had "destroyed the confidential status of the seven attorney-client communications by permitting their disclosure to the SEC staff."). *See also In re Qwest Communications Int'l, Inc.,* No. 06-1070, 2006 WL 1668246 (10th Cir. June 19, 2006); *United States v. Mass. Inst. Of Tech.*, 129 F.3d 681, 686 *(1st Cir. 1997); *Westinghouse Elec. Corp. v. Republic of the Phil.*, 951 F.2d 1414, 1422 (3d Cir. 1991); *In re Martin Marietta Corp.*, 856 F.2d 619, 623-24 (4th Cir. 1988); *In re John Doe Corp.*, 675 F.2d 482, 489 (2d Cir. 1982); *but see Diversified Industries, Inc. v. Meredith*, 572 F.2d (8th Cir. 1977) (upholding attorney-client privilege against a private litigant concerning documents previously disclosed to the SEC).

## V. Parallel proceedings

A. Background: Parallel proceedings generally involve a situation in which the Commission is conducting an investigation into conduct which may also be under inquiry by DOJ, other federal agencies, state law enforcement agencies, private entities such as the Public Accounting Oversight Board, and self-regulatory organizations.

1. As the *Manual* makes clear, the Supreme Court and a number of lower federal courts have concluded that there is nothing improper in conducting parallel proceedings. *Manual*, at 110, n. 8 (collecting cases).

2. Indeed, the securities laws seem to contemplate such proceedings. *See, e.g.*, Section 21(d), Securities Exchange Act of 1934.

3. Parallel proceedings offer efficiencies for the government and for practitioners.

4. These proceedings also offer pitfalls for the unwary. *See, e.g., U.S. v. Scrushy*, 366 F. Supp. 2d 1134 (D. Ala 2005).

5. The *Manual* specifically discusses parallel proceedings in Section 5.2.1.

B. Overview: The *Manual* discusses parallel proceedings largely in the context of SEC civil and DOJ criminal inquiries.

1. It encourages the staff to "coordinate their investigations with parallel criminal investigations when appropriate…"

2. The *Manual* cautions however that there are "unique set of circumstances" involved in parallel proceedings which must carefully be considered.

C. Key considerations: The *Manual* points out a number of key considerations the staff is directed to keep in mind.

1. The investigations must be independent: Here, the *Manual* cautions the staff that an investigation is not to be initiated to obtain evidence for a criminal prosecution, but for its own civil investigative purpose.

a. The staff must make its own independent decision about what documents and testimony to seek, the location of the testimony and similar matters.

b. The staff should not be seeking testimony or documents solely for criminal prosecutors. These points seem to be based on the district court decision in *U.S. v. Stringer*, 408 F. Supp. 2d 1093 (D. Or. 2006), despite the fact that the ruling was reversed on appeal.

2. Generally however, sharing information with prosecutors is permissible.

a. In some instances, it is appropriate for criminal prosecutors to request that the SEC refrain from taking actions that would harm the criminal inquiry.

b. In other instances, it may be appropriate for the SEC to request that the criminal prosecutors refrain from taking certain actions.

3. Questions by counsel about parallel criminal proceedings: The *Manual* codifies what has historically been staff practice.

a. If a practitioner inquiries about the existence of a parallel criminal inquiry the "Staff should direct counsel or the individual to the section of Form 1662 dealing with 'Routine Uses of Information' and state that it is the general policy of the Commission not to

comment on investigations conducted by law enforcement authorities responsible with enforcing criminal laws."

b. The Section goes on to note that "Staff should also invite any person who raises such issues to contact criminal authorities if they wish to pursue the question of whether there is a parallel criminal investigation."

c. If there is a request about whom to contact by counsel or the witness, the staff is directed by the *Manual* not to respond "unless authorized by the relevant criminal authorities." *Manual* at Section 5.2.1.[3]

D. Referrals by the SEC to other agencies: In many instances, parallel proceedings may arise from a referral by the SEC or because a matter has been referred to the Commission by another agency. Practitioners in this area should be mindful of this fact. because it can have a significant impact on the manner in which the investigation is approached.

1. Although the SEC considers its investigations to be confidential and nonpublic, it has authorized the staff by delegated authority "to grant access to nonpublic domestic and foreign governmental authorities, self-regulatory organizations and other specific persons." *Manual*, Section 5.1.

2. The "discussion rule": According to the *Manual* cooperation and coordination with other law enforcement agencies often requires the staff to discuss nonpublic information prior to the grant of formal access.

a. Rule 2, SEC's Rules Relating to Investigations, was adopted to permit these discussions. Those discussions must be authorized at the Assistant Director level or above.

b. Rule 2 does not authorize the staff to furnish nonpublic documents to other law enforcement authorities.

c. This Rule permits the staff to share investigative information in a wide variety of contexts, such as with the President's Financial Fraud Task Force**,** federal and state criminal prosecutors, and other federal and state law enforcement agencies.

3. Access: Section 24(c) and Exchange Act Rule 24c -1 authorizes the SEC to grant access to nonpublic information in its enforcement files.

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[3] The Section does not discuss the potential impact of parallel proceedings on the SEC's investigations. Clearly there is an impact, however. Frequently witnesses faced with parallel inquiries by the SEC, DOJ and perhaps others may decline to cooperate or provide testimony. Although the *Manual* does not discuss this point, it does contain a discussion of the Fifth Amendment and cooperation. There is also a reference to the Fifth Amendment in the Section on the Wells Process to the Fifth Amendment.

a. The *Manual* notes however, that "work product and other privileged information is rarely disclosed." This suggests that the Action Memoranda prepared by the staff for submission to the Commission to request the issuance of a formal order of investigation or the institution of an enforcement action and for similar matters is typically not transmitted to the agency granted access.

b. Under the Rule, a wide variety of law enforcement authorities can be granted access to SEC files including:

   i. Federal, state, local and foreign governmental authorities;

   ii. Self-regulatory and similar organizations;

   iii. Foreign financial regulatory authorities;[4]

   iv. SIPC and SIPC trustees;

   v. Trustees in bankruptcy;

   vi. Court-appointed counsel, and similar persons who perform functions arising from securities litigation such as receivers or trustees;

   vii. Professional licensing or oversight authorities; and

   viii. Agents, employees or representatives of such persons.

c. Procedure: Access requests must be in writing and signed by a senior official of the requesting authority.

   i. Enforcement has a standard form for this, which is not included in the *Manual*.

   ii. The Director of the Division of Enforcement has delegated authority to grant these requests. Section 3.2.6.4 notes that investigative files are to be maintained in a systematic way in part to facilitate granting access. Rule 30-4(a)(7) of the SEC's Rules of Organization delegates this authority to the Director. An access grant generally applies to existing information and information obtained in the future for those entities listed in Rule 24c-1(b).

[4] The Commission has Memoranda of Understanding with 39 foreign regulators. Under these agreements, the SEC coordinates and may share information with foreign regulators. In addition it may also enter into less formal arrangements in certain instances. *Id.*

iii. When an access request has been approved, a letter is sent to the requestor.

E. Informal referrals: In addition to the "discussion rule" and the formal referral process discussed above, there can also be "informal" referrals to federal or state criminal authorities, self-regulatory organizations, the Public Company Accounting Oversight Board, or state agencies.

1. According to Section 5.5, the staff has delegated authority to make informal referrals under a number of rules which include:

a. Rule 5(b), Informal and Other Procedures. This Rule provides in part that "The Commission may also, on some occasions, refer the matter to, or grant requests for access to its files made by, domestic and foreign governmental authorities or foreign securities authorities, self-regulatory organizations such as stock exchanges or the National Association of Securities Dealers, Inc. and other persons or entities."

b. Exchange Act Rule 24c-1 which provides in part that "The Commission may, in its discretion and upon a showing that such information is needed provide nonpublic information in its possession to any of the following persons if the person receiving such nonpublic information provides such assurances of confidentiality as the Commission deems appropriate…" The Rule goes on to list a wide variety of state and local law enforcement agencies as well as self regulatory authorities.

2. The *Manual* has specific subsections discussing informal referrals to criminal authorities, self regulatory organizations, the PCAOB, and professional licensing boards.

a. The criteria are generally the same in each instance;

b. Typically, the process must be made through a senior Enforcement official; and

c. The conduct at issue should be tied to the particular entity to which access is granted.

F. Parallel proceedings with the Division: In some instances, the SEC may authorize the initiation of enforcement action or an administrative proceeding while the Division of Enforcement continues its investigation. This situation can present significant parallel proceedings issues in view of the Commission's very broad investigative authority.

1. Section 3.13 of the *Manual* specifically provides that "The Division may continue to investigate and issue investigative subpoenas pursuant to the

formal order of investigation while simultaneously litigating a related civil action if there is an independent, good-faith basis for the continued investigation. An independent, good-faith basis may include the possible involvement of additional persons or entities in the violations alleged in the complaint, or additional potential violations by one or more of the defendants in litigation."

2. When there is a pending court proceeding, the *Manual* cautions the staff to exercise "judgment" when issuing investigative subpoenas. Considerations impacting that judgment include:

    a. The degree of factual and legal overlap;

    b. The prior course of the litigation;

    c. The likely response of defense counsel; and

    d. The likely views of the particular judge assigned to the case.

        i. There is "some case law" to support the practice of issuing investigative subpoenas. The "staff should not use investigative subpoenas solely to conduct discovery with respect to claims alleged in the pending complaint."

        ii. The *Manual* cautions that a court might find this practice to be a "misuse of the SEC's investigative powers and [that it] circumvents the court's authority and the limits on discovery in the Federal Rules of Civil Procedure."

3. If the investigative staff obtains "testimony or documents in the investigation that are properly discoverable in the litigation, the SEC must produce them in the litigation in accordance with the Federal Rules of Civil Procedure."

4. Before continuing an investigation or obtaining a formal order, the investigative team is cautioned to coordinate with "trial counsel" which presumably means SEC trial counsel, not defense counsel.

5. If there is a pending administrative procedure, restrictions on continuing the investigation are covered by Rule 230(g), Rules of Practice.

    a. The Division is required to notify the hearing officer and each party promptly that a subpoena has been issued under the same formal order; and

    b. The hearing officer is required to take whatever steps are necessary to ensure that the investigative subpoena is not issued for the purpose of obtaining evidence for the proceeding. In addition, the

hearing officer is authorized to provide documents obtained through such a subpoena to each respondent in the proceeding on a "timely basis."

G. Special considerations with SROs: Additional considerations apply to Self Regulatory Organizations such as the exchanges.

1. Background: Generally SROs are not "state actors" for constitutional purposes. Accordingly, constitutional privileges such as the Fifth Amendment may not apply during their inquiries. Indeed, SROs typically have a rule which requires that their members fully cooperate with their inquiries. Failure to cooperate can lead to expulsion. Failing to testify in their inquiries by invoking the Fifth Amendment can thus result in expulsion. *See, e.g.* http://sec.gov/litigation/litreleases/consentcsfb.pdf (NASD withdraws charges against investment banker who invoked Fifth Amendment after reversal of sanction by SEC and reversal of criminal conviction by Circuit Court).

a. In certain instances however, there may be limitations on these principles.

b. Recently there have been high profile cases raising this issue.

2. Section 3.1.4 of the *Manual* deals with parallel investigations and the state actor doctrine.

a. According to this section, the "state Actor Doctrine applies to a wide variety of private actions in which government is in some way concerned. It has been analyzed under a two-prong test, either of which can result in a finding of state action:"

i. Joint actions -- where the state and private entities take actions in concert; or

ii. Government compulsion -- where the private entity is encouraged to take certain actions by the governmental entities.

b. Where the state Actor Doctrine applies, the private entity, typically an SRO, may not be able to invoke its non-cooperation rule if the witness invokes his or her Fifth Amendment privilege.

c. The issue typically arises, according to this Section, when the witness invokes the Fifth Amendment privilege during SEC investigative testimony and is then summoned to testify before the private entity. In that instance the witness may not be able to assert the Constitutional protection or an adverse inference may be

drawn at trial. Under these circumstances, the staff is directed to consider the following guidelines:

i. In fact and appearance the SEC and private investigation should be parallel and not jointly conducted;

ii. The staff should "not take any investigative step principally for the benefit of the private entity's investigation or suggest investigative steps to the private entity"; and

iii. The staff is directed not to suggest any lines of questions or provide any documents for use in questioning the witness.

## VI. Documents and Testimony

A. Overview: Several directives in the *Manual* which are intended for the staff provide guidance to practitioners in representing a client before the Commission. Sections regarding the production of documents and regarding witnesses are instructive.

B. Producing documents. Typically, a request for information or testimony in either a formal or informal investigation begins with a request for documents. The request can be voluntary or pursuant to a subpoena.

1. Voluntary productions: These are typically used during informal investigations although as the *Manual* notes, the staff can also make an informal request during a formal investigation.

2. Creating documents: The *Manual* also notes that the "staff also may request the voluntary creation of documents, such as chronologies of events." *Id.* at Section 3.2.3. Although the staff has no authority to compel the creation of such documents, counsel may want to the consider the request

3. Required documents: Regulated entities are required to produce certain materials even without a subpoena. Under Sections 17(a) and (b) of the Exchange Act and Section 204 of the Advisers Act and the rules thereunder, regulated entities must furnish certain information to the staff, even absent a subpoena.

a. Some regulated entities have policies regarding notice to the customer.

b. In this regard, the *Manual* notes that the staff may want to "consider requesting that a firm not disclose the request for documents, at least for a certain limited period of time."

4. News media: There are special considerations for requests to news media. In 2006, the Commission issued a release detailing special procedures relating to news media. *See* 17 CFR §202.10.

5. The form of the production: Traditionally, document productions largely involved paper documents. Today, productions are frequently in electronic form. The *Manual* outlines procedures for producing documents which should be carefully considered when responding to a subpoena. These include:

    a. Preference for electronic format: The staff is encouraged to request that the documents be furnished in an electronic format and to include OCR text. The staff however, has the discretion to accept the production in paper format.

    b. Whether the production is in an electronic format or paper, the producer will be directed to preserve the originals.

    c. The producer should enclose a list briefly describing the documents produced. This "list should include the paragraph(s) in the subpoena attachment to which each item responds."

6. Cover letter: The production should be made with a cover letter which specifies:

    a. Whether all obligations under the subpoena have been met; and

    b. If all requested materials have been produced.

7. Withheld materials: If materials have been withheld or not produced the producer must:

    a. Provide a list of what is not being produced. The list should "describe each item separately, noting: its author(s); the date; its subject matter; the name of the person who has the item now, or the last person known to have it; the name of everyone who ever had the item or a copy of its, and the names of everyone who was told the item's contents; and the reason the subpoenaed entity or individual did not produce the tem." *Manual* at §3.2.6.2.

    b. If the item is withheld on a claim of privilege, then an appropriate privilege log must be furnished.

    c. If documents covered by the subpoena have been disguarded, destroyed or lost, they should be identified and the date on which they were lost, discarded or destroyed should be furnished.

8. Producing copies: The *Manual* provides that the "staff may allow a subpoenaed entity or individual to produce photocopies of the original documents. . . " In that instance, it provides guidelines for "acceptable productions" of copies:

    a. The copy must be identical to the original;

    b. There must be an identifying notation on each page such as the initials of the person and followed by a number in a blank corner;[5]

    c. If the document contains a removable flag or post-it, a copy of the document with and without the flag or post should be produced;

    d. In the case of multiple productions by the same source, it is suggested that a production date (month, date, year) be added; and

    e. The producer must maintain the original of all copied documents;

9. Electronic productions: This is the preferred method of document production.

    a. Format: The material can be scanned collections, e-mail or native files; the staff is directed not to take material in other formats;

    b. Organization: The material is to be organized by custodian;

    c. Summary: A summary of the number of records, images, emails, and attachments in the production should be provided to permit the staff to confirm that the complete production has been loaded onto the SEC computer;

    d. Software: Any electronic production should be compatible with Concordance 8.2, which the staff uses;

    e. Form: The data can be delivered on a CD, DVD or hard drive;

    f. Scanned collections: Each must contain four components:

        i. image file;

        ii. delimited text file;

        iii. optical character recognition (“OCR”) text; and

        iv. option cross-reference file.

[5] If originals are produced, the *Manual* directs that no identifying notations should be put on the documents.

g. E-mail: The preferable method is to convert them into a central repository or database that is searchable with Concordance. The preferred format is delimited text with images and native attachments. Alternative formats that are acceptable are PST (Microsoft Office) and NSF (Lotus Notes).

10. Privilege logs: Logs are covered by Section 3.2.6.2.4. The staff is directed to request a detailed privilege log for each document withheld on the basis of privilege. If sufficient information is not provided, it may constitute a waiver, according to the *Manual.*

a. The request: The staff is directed to include the specifics of what is required in the in a privilege log. The instruction directs the producing party to provide a list which includes the following for each document:

i. The identity and position of the creator;

ii. The creation date;

iii. the present or last known custodian;

iv. a brief description of the document including its subject matter;

v. the identity and position of all persons or entities known to have been furnished the document or a copy or informed of its substance;

vi. the reason the document is not being produced; and

vii. the specific request in the subpoena to which the document relates.

b. Confirmation: Following production the staff is directed to request confirmation that all the documents have been produced or are listed on the log;

c. Testimony: If the privilege is asserted in testimony, the staff is directed to stay on the record and take care in asking questions about the assertion and note that they are not seeking privileged material.

11. Metadata: The *Manual* only mentions metadata in the context of a discussion of accounting firm work papers. There, it states that "Many large accounting firms maintain and create their work papers electronically. Electronic work papers are often a rich source of meta data and may be easier to navigate than hard copies." *Id.* at p. 55. This may

suggest that companies should consider metadata in the context of their document retention policies.

12. Certifications: At the time of the production, the staff is directed to obtain a certification from the custodian regarding the records which complies with Rules 902(11) and 902(12) of the Federal Rules of Evidence. Standard forms are contained in the *Manual* for domestic and foreign records.

13. Completeness: If a party wants to settle, that party will be required to execute a certificate of completeness as to the document production:

    a. The certification will have to acknowledge that the SEC relied on the completeness of the production;

    b. It also must state that the party made a diligent search of all files in his or her possession, custody or control that are reasonably likely to contain requested records and the either all have been produced or listed on a privilege log. If the producing party is an entity, the certification should include a representation that a diligent inquiry of all persons who reasonably had possession of responsive documents has been made.

    c. The certification is to be used for productions which are voluntary or under subpoena.

C. Witnesses: The *Manual* discusses witnesses and taking testimony in Section 3.3. A number of sections are straightforward dealing with matters such as the dissemination of Privacy Act Warnings, Forms 1661 and 1662, going on and off the record, the availability of transcripts and the use of background questionnaires. Three key areas concern witness assurance letters, immunity orders and contacting the employees of issuers.

1. Witness assurance letters: Section 3.3.5.3.1 concerns witness assurance letters. These letters are used in "rare" instances when the SEC does "not intend to bring an enforcement action against him or her or an associated entity. In return, the witness agrees to provide testimony and documents and information." The letter must be authorized by the Commission.

    a. Key considerations include:

        i. Whether the SEC can obtain the testimony elsewhere;

        ii. Whether the witness can provide "crucial" evidence to an enforcement action against others; and

        iii. Based on what is known, whether the witness be a subject of a recommendation for an enforcement action?

b. The letter is based on "current information." Thus, the staff is required to create an inventory of materials at the time of the letter. The form letter in the *Manual* states that the letter is based on current information and notes that the witness is agreeing to cooperate completely and truthfully.

c. The form letter also notes that the SEC is agreeing not to use any statements made against the witness, but they may be shared with the proper authorities in the event of a perjury or obstruction referral.

d. No targets: Section 3.3.2 should also be considered, This Section specifies that unlike grand juries the Commission does not have "targets." It relies on the Supreme Court's decision in *SEC v. O'Brien,* 467 U.S. 735 (1984).

2. Immunity orders. Section 3.3.5.3.2 covers immunity orders. It notes that 18 U.S.C. §§6001-6004 provides that where certain criteria are met and upon approval of the Attorney General the SEC may issue an order granting immunity from criminal prosecution to a witness in an investigation and compelling his or her testimony and other information.

a. This issue arises where the witness asserts the Fifth Amendment;

b. The type of immunity granted is use immunity, which prohibits the government from using a witness's compelled testimony against the witness in connection with a criminal prosecution.

c. The staff does not have authority to grant immunity to any witness without the approval of the Attorney General and a Commission order.

d. Proffers: These are used in connection with an effort to obtain an immunity order or a witness assurance letter, *see also* Section 3.3.5.4. Generally, under these agreements, the witness meets with the staff and provides information which cannot be used against him or her except for later impeachment. A copy of a standard proffer agreement is included in the *Manual.*

3. Contacting employees of issuers. This topic is covered in Section 3.3.5.3.3. The staff is directed to comply with ABA Model Rule of Professional Conduct 4.2 which essentially provides that a lawyer can not communicate about the subject of the representation with a person known to be represented by another lawyer without the consent of that lawyer.

a. Absent a compelling reason, the staff should go through corporate counsel in contacting management such as senior officers, supervisors, employees whose acts can be imputed to the company

or those whose statements would constitute an admission of the entity;

b. If corporate counsel has not asserted that he or she represents any particular group of employees in the above listed groups, the staff can contact the person directly. When doing so, the staff should ask if the person is represented;

c. The staff can generally contact former employees without first contacting corporate counsel unless "corporate counsel . . . has affirmatively stated that corporate counsel has been retained by that particular former employee." This section cautions however, that if the staff contacts such an employee they cannot try to elicit information known to the person that is supposed to be confidential.

## VII. Conclusions

A. The new *Enforcement Manual* is a significant development. It adds transparency to enforcement procedures and contributes to the overall appearance of fairness regarding SEC enforcement investigations.

B. In part it details internal procedures for the staff. A review of those procedures gives the practitioner insights into the entire investigative process.

C. Key sections of the *Manual* focus on the Wells Process, parallel proceedings, privilege waivers and cooperation credit, the production of documents and testimony.

D. The *Manual* does not cover all Enforcement practices and policies. A glaring omission is the impact of asserting the Fifth Amendment on the Wells Process.

E. Overall, every practitioner in this area should carefully review the *Manual.*

Securities and Exchange Commission
Division of Enforcement


# Enforcement Manual

Office of Chief Counsel

*October 6, 2008*

Enforcement Manual
Table of Contents

# 1. Introduction

## 1.1 Purpose and Scope

The Enforcement Manual ("Manual") is an electronic document designed to be a reference for the staff in the U.S. Securities and Exchange Commission's ("SEC") Division of Enforcement ("Division" or "Enforcement") in the investigation of potential violations of the federal securities laws. It contains various general policies and procedures and is intended to provide guidance only to the staff of the Division. It is not intended to, does not, and may not be relied upon to create any rights, substantive or procedural, enforceable at law by any party in any matter civil or criminal.

## 1.2 Origin

The Manual was prepared under the general supervision of the Division of Enforcement's Office of Chief Counsel ("OCC") in consultation with the Securities and Exchange Commission's Office of the General Counsel ("OGC"), Office of the Inspector General ("OIG") and Office of the Chairman. OCC coordinates periodic revision of the Manual. Although the Manual is intended to be comprehensive, decisions about specific investigations, cases, and charges are made according to the specific facts and circumstances at hand.

## 1.3 Public Disclosure

The Manual is United States Government property. It is to be used in conjunction with official duties. All materials contained in the Manual are subject to the provisions of Title 5, U.S.C. Section 552(a)(2), with the exception of those materials excluded under 17 C.F.R. Section 200.80. Accordingly, this Manual is available for public inspection on line at www.sec.gov.

## 1.4 Fundamental Considerations

### 1.4.1 Mission Statement

The Division's mission is to protect investors and the markets by investigating potential violations of the federal securities laws and litigating the SEC's enforcement actions. Values integral to that mission are:

- Integrity: acting honestly, forthrightly, and impartially in every aspect of our work.

- Fairness: assuring that everyone receives equal and respectful treatment, without regard to wealth, social standing, publicity, politics, or personal characteristics.

- Passion: recognizing the importance of and caring deeply about our mission of protecting investors and markets.

- Teamwork: supporting and collaborating with colleagues and other Divisions and Offices at the SEC and fellow law enforcement professionals.

### 1.4.2 Updating Internal Systems

The Division uses several internal systems, including the Hub, CATS, and Phoenix, to help manage case information and track both the collection and distribution of disgorgement and penalties. The reliability and usefulness of each of the Division's internal systems is dependent upon timely and accurate entry of information by the staff. Therefore, it is considered "mission critical" to keep all information required by these systems updated in real time. Staff at all levels of the Division are required to adhere to the data entry requirements of each system.

### 1.4.3 Consultation

Although this Manual is intended to be a reference for the staff in the Division who are responsible for investigations, no set of procedures or policies can replace the need for active and ongoing consultation with colleagues, other Divisions and Offices at the SEC, and internal experts. Investigations often require careful legal and technical analysis of complicated issues, culminating in difficult judgment calls that may affect market participants, individuals, and issuers. Therefore, any time an issue arises for which colleagues or other Divisions or Offices may hold particular expertise, the staff should consider consultation. In addition, staff should keep other Divisions and Offices informed regarding issues of interest that arise during investigations, and consult with interested Divisions and Offices before making recommendations for action to the Commission at the conclusion of an investigation.

### 1.4.4 Ethics

Maintaining and fostering of a culture of integrity and professionalism is the Division's highest priority. The Office of Government Ethics' ("OGE") "Standards of Ethical Conduct for Employees of the Executive Branch" lays out the basic obligation of public service: "Each employee has a responsibility to the United States Government and its citizens to place loyalty to the Constitution, laws and ethical principles above private gain. To ensure that every citizen can have complete confidence in the integrity of the Federal Government, each employee shall respect and adhere to the principles of ethical conduct… ." *See* 5 C.F.R. Part 2635.101 The SEC has a number of resources from which any and all Division staff can obtain guidance on questions regarding ethical conduct. Prominent among the resources available are the SEC ethics officials. Staff should not hesitate to consult with the Division Chief Counsel, the Deputy Ethics Liaison Officer or the attorney staff in the SEC Ethics Office on any question of ethics. Also available to staff are the written Ethics bulletins and reference of applicable statutes available from the SEC Ethics Office.

Considerations:

- Should staff find themselves in doubt over an ethical issue, staff should seek guidance on the issue from an SEC ethics official *before* acting.

- Staff should remain alert to new rules and updates posted by the Ethics Office.

- Staff should be aware of ethical issues that may arise, including policies on:

    - Confidentiality and the Protection of Non-public Information
    - Attorney Responsibility (under the OGE Standards of Ethical Conduct for Employees of the Executive Branch, the Rules of Professional Responsibility of the state in which the attorney is licensed to practice law, and the Rules of Professional Responsibility of the state in which the attorney is appearing on behalf of the Commission before a tribunal or otherwise engaging in such other behavior as may be considered the practice of law under that state bar's ethical and disciplinary rules.)
    - Securities Transactions by Employees
    - Conflict of Interest (including Financial and Personal Interests)
    - Recusals (including the one year recusal policy for Division staff)
    - Referral of Professional Misconduct
    - Publication Guidelines
    - Gifts and Invitations
    - Outside Employment and Activities
    - Requirements under the Hatch Act
    - Misuse of Public Office for Private Gain
    - Pro Bono Activity
    - Seeking and Negotiating Employment Outside the SEC

Further Information:

- *See also* OGE Standards of Ethical Conduct for Employees of the Executive Branch 5 CFR Part 2635 *et al*.
- OGE Compilation of Federal Ethics Laws available at *http://www.usoge.gov/pages/laws_regs_fedreg_stats/compilation_ethics_laws.html*
- Criminal Conflict of Interest Statutes including 18 U.S.C Sections 203,205,207,208, 209 and Other Related Statutes available at *http://www.usoge.gov/pages/laws_regs_fedreg_stats/other_ethics_guidance.html*

## 2. A Guide to Matters Under Inquiry ("MUIs") and the Stages of Informal and Formal Investigations

### ` 2.1 General Policies and Procedures

#### 2.1.1 Ranking Investigations and Allocating Resources

Introduction:

The Division of Enforcement handles a number of investigations which vary in their size, complexity, and programmatic importance. Devoting appropriate resources to investigations which are more significant will help ensure high quality investigations and maximize desired program outcomes. In quarterly reports to the Director, Home Office Associate Directors and Regional Directors list their top ten investigations and rank their top three investigations. The top three investigations are ones which he or she considers to be critically important, while the top ten are considered significant. To achieve consistency in this area, Home Office Associate Directors and Regional Directors should take into account certain criteria when ranking their top three investigations and listing their top ten investigations so that they may effectively make decisions regarding resource allocation among all competing investigations.

Considerations When Ranking an Investigation:

To determine their top three and top ten investigations, Home Office Associate Directors and Regional Directors should evaluate at least three factors for each investigation under their responsibility:

- the programmatic importance of an enforcement action, considering:
    - whether the subject matter is an SEC priority
    - whether the subject matter is a Division priority
    - whether an action would fulfill a programmatic goal of the SEC or the Division
    - whether an action would address a problematic industry practice
    - whether the conduct undermines the fairness or liquidity of the U.S. securities markets
    - whether an action would provide an opportunity for the SEC to address violative conduct targeted to a specific population or community that might not otherwise be familiar with the SEC or the protections afforded by the securities laws
    - whether an action would present a good opportunity to coordinate with other civil and criminal agencies

- whether the conduct can be addressed by any other state or federal regulators
- whether an action would alert the investing public of a new type of securities fraud

- the magnitude of the potential violations involved in the investigation, considering:
    - the egregiousness of the conduct
    - the length of time the conduct continued, or whether it is ongoing
    - the number of violations
    - whether recidivists were involved
    - whether violations were repeated
    - the amount of harm or potential harm to victims
    - the amount of ill-gotten gains to the violators
    - whether victims were specifically targeted based on personal or affinity group characteristics
    - for issuers or regulated entities, whether the conduct involved officers, directors, or senior management
    - whether gatekeepers (such as accountants or attorneys) or securities industry professionals are involved

- the resources required to investigate the potential violations, considering:
    - the complexity of the potential violations
    - the approximate staff hours required over the course of the investigation
    - the number of staff assigned
    - the amount of travel required
    - the duration of the relevant conduct
    - the number of potential violators
    - the number and location of potential witnesses

- the number and location of relevant documents to be reviewed

Although determining the overall significance of the investigation should take the factors above into consideration, the ranking of an investigation is a judgment to be made by the Home Office Associate Directors and Regional Directors, based on all facts and circumstances known to date. For example, an investigation ranked in the top three might include a complex investigation into a potentially egregious accounting fraud that has a very high resource requirement (and the longest amount of time needed to complete the investigation). However, an investigation into a potential market manipulation that may result in a trading suspension might also rank in the top three, despite the lower amount of resources needed, the shorter time needed to complete the investigation, and the smaller number of harmed investors because the conduct is egregious and requires urgent action.

Considerations When Allocating Resources Among Investigations:

Allocating resources among investigations requires that Associate and Assistant Directors[1] exercise flexibility and creativity. Associate and Assistant Directors will normally assign staff to more than one investigation at a time, specifying the priorities of competing investigations so that staff members may plan their work.

Priorities among investigations may change rapidly depending on the stage of the investigation. For example, two significant investigations may compete for resources, but staff may be assigned to review and analyze evidence in one investigation while waiting for documents to be produced in another investigation. Therefore, when allocating resources among competing investigations, Associate and Assistant Directors should take into account not only the significance of the investigation, but the phase of the investigation, considering, among other things:

- whether there is an urgent need to file an Enforcement action, such as an investigation into ongoing fraud or conduct that poses a threat of imminent harm to investors

- the volume of evidence that the staff must collect and review, such as trading records, corporate documents, and e-mail correspondence

- the level of analysis required for complex data and evidence, such as auditor workpapers, bluesheets, or financial data

- the number and location of witnesses and the scheduling of the testimony

- travel requirements

[1] The term "Assistant Directors" includes Assistant Directors in the Home Office and Assistant Regional Directors in the Regional Offices.

- timelines for writing internal memos, evaluation of the case by pertinent SEC Offices and Divisions, and consideration of the matter by the Commission

- coordination with and timing considerations of other state and federal authorities

For investigations ranked in the top three, Associate and Assistant Directors should consider assigning a minimum of two permanent staff attorneys to ensure that there is continuity on the investigation in the event of absences or staff transitions. In addition, the assignment of at least two attorneys may contribute to a collaborative approach that improves the quality of the investigation and promotes accountability. Additional attorneys may be assigned depending on the phase of the investigation.

### 2.1.2 Six-Month Review of Investigations and Status Updates

Introduction:

Each investigation, whether formal or informal, should be reviewed by the assigned staff (Assistant Director level and below) at each six-month mark after the investigation is opened. In addition to the staff's continuing entry of information into the Hub (including, for example, adding the names of new staff assigned to the investigation and removing the names of staff no longer assigned), the status of the information should be checked and a narrative update should be entered into the Hub at the six-month mark. Although each investigation is unique and does not conform to a particular time frame, the six-month reviews and updates will allow senior management (Associate Director level and higher) to assess the progress of an investigation and evaluate whether the investigation continues to be an appropriate allocation of resources.

Basics:

- The assigned staff should review the investigation and update the status of an ongoing investigation on each six-month anniversary of the opening date of the investigation.

- The narrative update on the Hub system should be included in the "Current Summary" narrative box under the "Nature/Substance of Case" tab for their investigation. In addition, the staff should submit the text of the update to a Deputy Director by e-mail.

- The narrative in the Hub should explain any change in the original analysis contained in the case opening narrative regarding whether the investigation is an appropriate use of resources. In particular, the assigned staff should keep in mind whether the conduct is still within the statute of limitations period.

- The narrative should note the stage of the investigation and any major events or milestones that have occurred in the prior six months. For example, the staff

might note that they are taking testimony, that they are conducting settlement negotiations, or that a potential defendant has been indicted.

- The six-month review should include a review of information entered into the Hub concerning the investigation. Any inaccurate or out-of-date information should be corrected.

Exception:

An update is not required if an investigation is open, but is inactive because a civil action, administrative proceeding, or other event is in progress and the collection of information under the investigation has ceased. However, if an investigation is ongoing despite the filing of a civil action or the institution of an administrative proceeding (for example, if the investigation is ongoing as to persons not named in the action), then the staff must continue to update the status of the ongoing portion of the investigation.

## 2.2 Complaints, Tips, and Referrals

### 2.2.1 Complaints and Tips From the Public

Public complaints and tips are primarily received through the Division's e-mail address (enforcement@sec.gov), the SEC's online web form (http://www.sec.gov/complaint.shtml), or through contact with staff at any of the SEC's offices. The vast majority of complaints and tips received by the Division are in electronic form and the Division encourages the public to communicate with it through electronic media. Every complaint is carefully reviewed by Division staff for apparent reliability, detail and potential violations of the federal securities laws. After review, the complaint or tip generally is processed according to the guidelines below.

Guidelines for Processing of Public Complaints and Tips:

- Complaints that appear to be serious and substantial are usually forwarded to staff in the home office or the appropriate regional office for more detailed review, and may result in the opening of a MUI.

- Complaints that relate to an existing MUI or investigation are generally forwarded to the staff assigned to the existing matter.

- Complaints that involve the specific expertise of another Division or Office within the SEC are typically forwarded to staff in that particular Division or Office for further analysis.

- Complaints that fall within the jurisdiction of another federal or state agency are forwarded to the SEC contact at that agency.

- Complaints that relate to the private financials affairs of an investor or a discrete investor group are usually forwarded to the Office of Investor Education and Advocacy ("OIEA"). Comments or questions about agency practice or the federal securities laws are also forwarded to OIEA.

### 2.2.2 Other Referrals

#### 2.2.2.1 Referrals from FinCEN or Referrals Involving Bank Secrecy Act Material

The Bank Secrecy Act ("BSA"):

The BSA is a tool that the U.S. government uses to fight money laundering and drug trafficking. Enacted in 1970 and amended by the USA PATRIOT Act, it is designed to prevent financial institutions, including broker-dealers, from being used as vehicles through which criminals hide the transfer of illegally obtained funds. The recordkeeping and reporting requirements of the BSA create a paper trail for federal, state and local law enforcement to investigate the movement of funds in money laundering and other illegal schemes. The BSA is codified at 31 U.S.C. 5311, *et seq*. The regulations implementing the BSA are located at 31 C.F.R. Part 103.

For the SEC, the primary mechanism for enforcing compliance by brokers and dealers with the requirements of the BSA is Section 17(a) of the Securities Exchange Act of 1934 ("Exchange Act") and Rule 17a-8. Under Rule 17a-8, every registered broker or dealer must comply with the reporting, recordkeeping and record retention provisions of 31 C.F.R. Part 103. In the investment company context, the registered "funds" must comply with Rule 38a-1 of the Investment Company Act of 1940 ("Investment Company Act"). Rule 38a-1 states that funds must adopt and implement written policies and procedures reasonably designed to prevent violation of the "Federal Securities Laws." As defined in the Investment Company Act, "Federal Securities Laws" include the BSA.

BSA information is highly confidential, and subject to the strict limitations set out by the Financial Crimes Enforcement Network ("FinCEN"), a bureau in the Department of the Treasury. Enforcement staff has access to and reviews certain electronic reports filed under the BSA.

The Basics of Handling Referrals Containing BSA Material:

- FinCEN has determined that BSA materials are non-public documents and that, absent certain circumstances, these materials are privileged documents. Absent certain circumstances, staff is restricted by law from disseminating BSA material in litigation or to the public. However, staff may use the information contained in the BSA material as a lead to possible *underlying* documents of value in an investigation. All hardcopy BSA material should be segregated and kept under lock and key or if in electronic form, in a secure electronic file.

- BSA material may include, among other documents, Suspicious Activity Reports ("SARs"); Currency Transaction Reports ("CTRs") and Currency Transaction Reports by Casinos ("CTRCs") (i.e., reports on transactions in excess of $10,000); Reports of Foreign Bank and Financial Interests ("FBARs"); Reports of International Transportation of Currency or Monetary Instruments ("CMIRs"); and Reports of Cash Payments Over $10,000 Received in Trade or Business.

Considerations:

Please keep in mind the following considerations when receiving information from FinCEN or other sources that may contain BSA material:

- Does the referral contain BSA material? If so, staff should take appropriate steps to segregate and properly secure the material.

- Staff is permitted to share the information contained in BSA material with other SEC staff if relevant to an inquiry or investigation. Staff should not make copies or forward electronic copies of BSA information, particularly SARs, which are highly sensitive documents. Staff generally should not disclose BSA information or its existence to persons who may be assisting in a matter, such as an Independent Compliance Person, or Receiver because BSA materials are non-public documents. BSA materials cannot be shown to witnesses or marked as exhibits in testimony.

- BSA materials may be embedded within a document production. Therefore, staff should add the following language to its letter requests for documents to regulated entities and its subpoenas to financial institutions:

  **"If the document production contains Bank Secrecy Act materials, please segregate and label those materials within the production."**

Further Information:

- Staff should contact the Office of Chief Counsel for further information about how to handle BSA materials received from FinCEN or other sources.

- *See also* Section 4.7 of the Manual.

#### 2.2.2.2 Referrals from the Public Company Accounting Oversight Board

The Basics of Receiving a Tip from the PCAOB:

The enforcement staff of the Public Company Accounting Oversight Board ("PCAOB") may forward tips it receives to the staff of the Division of Enforcement. This is normally done through the Enforcement Chief Accountant's office, which makes

an initial assessment regarding whether future investigation is warranted. If the staff receives a referral through the office of the Chief Accountant of Enforcement:

- Staff and their supervisors should notify the office of the Chief Accountant of Enforcement about obtaining documents and information regarding the tip.

- If appropriate, staff should then get approval to open a MUI on the matter (*see* Section 2.3.1 of the Manual regarding Opening a MUI).

Considerations:

Consider calling the enforcement staff of the PCAOB to discuss the tip with them.

Further Information:

Please refer any questions about receiving a tip from the PCAOB to the Chief Accountant of the Enforcement Division.

### 2.2.2.3 Referrals from State Securities Regulators

The Basics of Receiving Referrals from State Securities Regulators:

State securities regulators enforce state-wide securities laws known as "blue sky laws." The Division of Enforcement receives information and referrals from state securities regulators. Most of the state securities regulators have relationships with the SEC regional office which covers the territory in which they are located and the state regulators direct their referrals to that office. Pursuant to Rule 2 of the SEC's Rules Relating to Investigations, the staff can share nonpublic information, including whether the staff has or will commence an investigation, with state regulatory agencies. 17 C.F.R. Section 203.2.

Considerations:

- Staff should discuss the information received from state securities regulators promptly with their supervisors.

- Consider ongoing coordination with the state securities regulator, as appropriate.

Further Information:

- If the opening of a MUI is appropriate, see Section 2.3.1 of the Manual.

### 2.2.2.4 Referrals from Congress

The Basics of Receiving a Referral from Congress:

The SEC frequently receives complaints and other information from members of Congress on behalf of the constituents whom they represent. Most of these letters are directed to the Office of Legislative Affairs or the Chairman's Office and then assigned to the appropriate SEC division or regional office. The Chairman's Office tracks the responses to congressional letters and has issued guidelines to follow concerning the style and format of congressional response letters. As with complaints and other information received from other sources, each complaint and tip received by the Division from Congress and congressional constituents is carefully reviewed by staff.

Considerations:

- Staff should not share nonpublic information, including whether the staff has or will commence an investigation, with the complainants or members of Congress.
- Staff should provide timely responses to congressional letters, meeting the deadlines required by the Office of Legislative Affairs or the Chairman's Office.
- If staff believes the information obtained from the congressional letter warrants the opening of a MUI, staff should follow the instructions for opening a MUI in Section 2.3.1 of the Manual.

Further Information:

Staff should consult the guidelines from the Office of Legislative Affairs and the Chairman's Office when drafting responses to congressional correspondence.

### 2.2.2.5 Referrals from Self Regulatory Organizations

The Basics of Receiving Referrals from SROs

The Division's Office of Market Surveillance ("OMS") is the primary point of contact for trading-related referrals by domestic Self Regulatory Organizations ("SROs"). Each equity and option exchange is responsible for monitoring its own markets and enforcing exchange rules and regulations and the federal securities laws. If the SRO discovers violative conduct and believes that it has jurisdiction, it will conduct its own investigation. If the SRO determines that it does not have jurisdiction over the parties involved in the matter, it will refer the potential violations to the SEC via the SRO Market Surveillance Referral System ("SMSR"). OMS reviews all SRO referrals and in consultation with senior staff in Enforcement opens MUIs and distributes the cases to the appropriate staff in the regional and home offices.

Considerations:

- Assigned staff should discuss information received from SROs with OMS.

- Consider ongoing consultation with SROs, as appropriate.

Further Information:

If the referring SRO continues with a parallel investigation, please refer to the policy on parallel investigations in Section 3.1.4 of the Manual.

## 2.3 Matters Under Inquiry ("MUIs") and Investigations

### 2.3.1 Opening a MUI

Introduction

The purpose of the procedures and policies for the review and approval of new MUIs is to help ensure efficient allocation of resources.

Opening a MUI requires that the staff assigned to a MUI (at the Assistant Director level and below) first conduct preliminary analyses to determine: 1) whether the facts underlying the MUI show that there is potential to address conduct that violates the federal securities laws; and 2) whether the assignment of a MUI to a particular office will be the best use of resources for the Division as a whole. If the preliminary analyses indicate that a MUI should be opened, then the staff, after consulting with the assigned Associate Director or Regional Head of Enforcement, should follow the procedures below for opening a MUI within the internal system and seeking the final approval of both the assigned Associate Director/Regional Head of Enforcement and a Deputy Director of the Division. Prior to any other considerations, the staff should consult NRSI and the Hub for related investigations. If a related investigation is found, the staff assigned to that investigation should be consulted.

Prior to opening a MUI, the assigned staff (Assistant Director and below) should determine whether the known facts show that an Enforcement investigation would have the potential to address conduct that violates the federal securities laws. The Division receives information from a variety of sources that may warrant the opening of a new MUI, including newspaper articles, complaints from the public, whistleblowers, and referrals from other agencies or self-regulatory organizations ("SRO"). Assigned staff are encouraged to use their discretion and judgment in making the preliminary determination of whether it is appropriate to open a MUI. The considerations described below are suggestions only and should not discourage the opening of a MUI based on partial information. MUIs are preliminary in nature and typically involve incomplete information. The threshold determination for opening a new MUI is low because the purpose of a MUI is to gather additional facts to help evaluate whether an investigation would be an appropriate use of resources.

To determine whether to open a MUI, the staff attorney, in conjunction with the Branch Chief and Assistant Director, should consider whether a sufficiently credible source or set of facts suggests that a MUI could lead to an enforcement action that would address a violation of the federal securities laws. Basic considerations used when making this determination may include, but are not limited to:

- The statutes or rules potentially violated;
- The egregiousness of the potential violation;
- The potential magnitude of the violation;
- The potential losses involved or harm to an investor or investors;
- Whether the potentially harmed group is particularly vulnerable or at risk;
- Whether the conduct is ongoing;
- Whether the conduct can be investigated efficiently and within the statute of limitations period; and
- Whether other authorities, including federal or state agencies or regulators, might be better suited to investigate the conduct.

After determining that a MUI has the potential to address conduct that violates the federal securities laws, the assigned staff should evaluate whether from a resources standpoint, it is reasonable for their office to handle the investigation. Basic considerations used when making this determination may include, but are not limited to:

- The location of the wrongful conduct;
- The location of the potential wrongdoers;
- The location of the issuer's, entity's, or SRO's headquarter;
- The location of most witnesses or victims; and
- The resources and expertise of the office.

If an office believes it has compelling reasons to handle a MUI or investigation for which another office may have a substantial nexus, it should consult with the other office to determine which office should pursue the MUI or investigation. Exceptions to the general guidance include:

- *Relation to a previous investigation*: If a MUI is closely related to a previous investigation, a determination should be made whether the office that handled

the previous investigation should handle the new MUI, regardless of whether that office has a nexus to the new MUI.

- *Insufficient resources to investigate*: The home office may open a MUI when a regional office has a nexus if that regional office determines that it cannot devote sufficient resources to pursuing the MUI or if the regional office has other concerns that prevent it from pursuing the matter.

If it later becomes clear that the MUI or investigation is centered in a specific region, consideration should be given to referring the investigation to that regional office, depending on available staff in the regional office and the stage of the investigation. In some situations, such as where witnesses are dispersed or where an office has special expertise, it may make sense for staff from more than one office to work together on a matter.

Procedures for Opening a MUI

If the preliminary analyses above suggest the potential to address conduct that violates the federal securities laws:

1) The assigned staff should consult with the assigned Associate Director/Regional Head of Enforcement concerning the analyses.
2) The staff attorney should fill out the electronic MUI form located in the Division's internal systems.
3) The form will be submitted electronically to the assigned Associate Director/Regional Head of Enforcement for approval.
4) The Associate Director/Regional Head of Enforcement should review the form promptly (within two business days), and, if he or she is satisfied that the MUI has the potential to address violative conduct, he or she may approve the MUI through the electronic form.
5) If the Associate Director/Regional Head of Enforcement approves the MUI form, the assigned staff should draft and send an e-mail message to a Deputy Director with a brief explanation regarding the MUI's potential to address violative conduct, and explain why this group is the appropriate one to handle the investigation from a resources standpoint.
6) The Deputy Director should review the e-mail promptly (within two business days) to determine whether, based on the staff's representations, the opening of the MUI is an appropriate use of resources.
7) If the Deputy Director agrees that the MUI is an appropriate use of resources, the Deputy Director may approve the opening of the MUI by e-mail to the Associate Director/Regional Head of Enforcement and assigned staff.
8) The assigned staff should maintain a copy of the correspondence and approval from the Deputy Director in the MUI files.

9) If the MUI requires expedited approval, and the assigned Associate Director/Regional Head of Enforcement is not available to approve the electronic MUI form, then the staff may use the MUI form to request approval from any available Associate Director/Regional Head of Enforcement. Alternatively, the staff may use the MUI form to request approval directly from a Deputy Director.

10) The Deputy Director will receive a weekly report of all MUIs opened during the prior week.

Considerations:

The internal system will convert a MUI to an investigation when the MUI has been open for sixty days. A reminder of the upcoming conversion is automatically generated and sent by e-mail to the primary staff member listed on the MUI form ten days prior to conversion and five days prior to conversion. Upon receiving the first reminder, and prior to the sixtieth day of the MUI, the staff should determine whether conversion to an investigation is appropriate. Staff should follow the policies and procedures for closing a MUI, or converting a MUI in Section 2.3.2 of this Manual.

Further Reference:

For more information on filling out MUI forms, please check for instructions on the internal tracking systems or contact a Case Management Specialist.

### 2.3.2 Opening an Investigation, Converting a MUI, or Closing a MUI

Introduction

Investigations are opened in two ways: 1) the investigation is opened when a MUI is converted to an investigation (which occurs automatically sixty days after the MUI is opened), or, 2) an investigation is opened independently, either prior to the sixtieth day automatic conversion of a MUI or without any history of a MUI in the case. In both cases, the opening of an investigation requires that the assigned staff (at the Assistant Director level and below) conduct an evaluation of the facts to determine the investigation's potential to address conduct that violates the federal securities laws. The analysis for whether to convert a MUI to an investigation, or open an investigation, differs from the analysis for whether to open a MUI. While a MUI can be opened on the basis of very limited information, an investigation generally should be opened after the assigned staff has done some additional information-gathering and analysis. It may also be appropriate at this time to revisit whether the office has a nexus to the MUI.

Analysis: Will the Investigation Have the Potential to Substantively and Effectively Address Violative Conduct?

The assigned staff, in consultation with the assigned Associate Director, should evaluate the information gathered to determine whether it is an appropriate use of resources to open an investigation (either through conversion of the MUI or independent

of a MUI). While the threshold analysis for opening of MUI is relatively low, determining whether the MUI should be converted to an investigation or whether to open an investigation is typically a more detailed evaluation that is based on additional information.

The evaluation for whether to convert a MUI to an investigation (or open an investigation) turns on whether, and to what extent, the investigation has the potential to address violative conduct. Threshold issues to consider when evaluating the facts include:

1) Do the facts suggest a possible violation of the federal securities laws involving fraud or other serious conduct?
2) If yes, is an investment of resources by the staff merited by:
    a) the magnitude or nature of the violation,
    b) the size of the victim group,
    c) the amount of potential or actual losses to investors,
    d) for potential insider trading, the amount of profits or losses avoided, or
    e) for potential financial reporting violations, materiality?
3) If yes, is the conduct:
    a) ongoing, or
    b) within the statute of limitations period?

In addition to the threshold issues above, one way to determine whether the conduct is serious is to consider the following supplemental factors:

- Is there a need for immediate action to protect investors?
- Does the conduct undermine the fairness or liquidity of the U.S. securities markets?
- Does the case involve a recidivist?
- Has the SEC or Division designated the subject matter to be a priority?
- Does the case fulfill a programmatic goal of the SEC and the Division?
- Does the case involve a possibly widespread industry practice that should be addressed?
- Does the matter give the SEC an opportunity to be visible in a community that might not otherwise be familiar with the SEC or the protections afforded by the securities laws?
- Does the case present a good opportunity to coordinate with other civil and criminal agencies?

Considerations

Assigned staff is encouraged to revisit whether the office still has a sufficient nexus under the new facts learned during the period of the MUI. If the facts have changed, assigned staff should consider whether it is appropriate to contact another office that may be better suited to handle the investigation.

Procedures for Converting a MUI to an Investigation

Sixty days after a MUI is opened, the MUI will be converted to an investigation unless the MUI is closed prior to the sixty day mark. The person listed as the primary staff on the MUI form will receive an automatic e-mail reminder ten days prior to the conversion of the MUI, and will receive a second e-mail reminder five days prior to the conversion of the MUI. Upon receiving the ten-day reminder e-mail:

1) The assigned staff, in consultation with the assigned Associate Director, should evaluate the facts gathered during the MUI, using the factors listed above, to determine whether, and to what extent, the investigation will have the potential to address violative conduct.

2) If the assigned staff, in consultation with the assigned Associate Director, determine that it is appropriate to proceed with the investigation, then the conversion to an investigation will occur without further action by the staff attorney, Branch Chief, or Assistant Director.

3) At the time of the conversion, the assigned staff should draft and submit an Opening Narrative Form to their Case Management Specialist including a brief statement regarding the investigation's potential to address violative conduct. The information included in this form will be included in the CATS file and available to the Deputy Director for review on a weekly basis.

4) If the assigned staff, in consultation with the assigned Associate Director, determine that the investigation does not have the potential to address violative conduct, or there is another reason that the investigation would be an inappropriate use of resources, then the assigned staff, in consultation with the assigned Associate Director, should close the MUI before it converts to an investigation. To close the MUI, the assigned staff should contact their Case Management Specialist, request to close the MUI, and provide an explanation for closing the MUI. Please refer to the internal system instructions for the closing MUI codes. If the MUI is not closed before its conversion to an investigation, then the investigation closing procedures must be followed (see Section 2.6 of the Manual).

Procedures for Opening an Investigation, Independent of a MUI

In certain circumstances, it is appropriate to open an investigation without having opened a MUI (for example, in a case in which emergency action is necessary), or convert a MUI to an investigation prior to the occurrence of the automatic conversion on the sixtieth day of the MUI. To open an investigation under these circumstances:

1) The assigned staff should consult with the assigned Associate Director concerning the analyses described above.

2) The staff attorney should fill out the investigation opening form in the internal system (CATS) and forward it, along with the Opening Narrative Form, to their Associate Director for approval.

3) The Associate Director should review the forms promptly (within two business days), and, if the Associate Director is satisfied that it is appropriate to proceed, the Associate Director may approve the opening of the investigation.

4) The staff attorney should forward the approved form to their Case Management Specialist for processing.

5) The assigned staff should draft and send an e-mail message to a Deputy Director with a brief explanation regarding the investigation's potential to address violative conduct and the office nexus.

6) If the Deputy Director agrees that the investigation is an appropriate use of resources, the Deputy Director may approve the opening of the investigation by e-mail to the Associate Director and assigned staff.

7) The assigned staff should maintain a copy of the correspondence with the Deputy Director in the investigation files.

8) If the investigation requires expedited approval due to ongoing conduct or imminent investor harm, and the assigned Associate Director is not available to approve the investigation opening form, then the staff may request approval from any available Associate Director. Alternatively, the staff may request approval directly from a Deputy Director.

9) The Deputy Director will receive a weekly report of all investigations opened during the prior week.

### 2.3.3 Formal Orders of Investigation

Under Rule 5(a) of the SEC's Informal and Other Procedures, the Commission "may, in its discretion, make such formal investigations and authorize the use of process

as it deems necessary to determine whether any person has violated, is violating, or is about to violate any provision of the federal securities laws or the rules of a self-regulatory organization of which the person is a member or participant." 17 C.F.R. Section 202.5 (a). Once the Commission issues a Formal Order of Investigation ("Formal Order"), members of the staff designated by the Formal Order to act as officers of the Commission for the purposes of the investigation may administer oaths and compel testimony and the production of evidence, among other things. Investigations are non-public unless otherwise ordered by the Commission. *Id.*

### 2.3.4 Formal Order Action Memo Process

Introduction**:**

The staff cannot issue investigative subpoenas to compel testimony or the production of documents unless the Commission issues a formal order of private investigation. The Commission may issue a formal order of investigation, in its discretion, if it deems that a violation of the federal securities laws may have occurred or may be occurring and a formal investigation is appropriate and necessary. The formal order serves two important functions. First, it generally describes the nature of the investigation that the Commission has authorized, and second, it designates specific staff members as officers for the purposes of the investigation and empowers them to administer oaths and affirmations, subpoena witnesses, compel their attendance, take evidence, and require the production of documents and other materials. Formal investigative proceedings are non-public unless otherwise ordered by the Commission.

Basics of Recommending that the Commission Issue a Formal Order:

The staff may recommend that the Commission issue a formal order by presenting an action memorandum to the Commission:

- The memo should describe known facts surrounding the potential violation, identify the persons and entities involved, describe the potential violations, discuss the stage of the investigation and the need for a formal order, and highlight any special issues or exigent circumstances.

- Before sending a formal order action memo to the Commission for consideration, the staff should circulate the memo to other interested Divisions and Offices for their review, erring on the side of over-inclusiveness. This review may help to identify potential issues at an early stage of the investigation that can make the investigation more effective.

- The Commission typically considers formal order matters during Closed Meetings (*see* Section 2.5.2.1 of the Manual). Urgent matters may be considered by the Duty Officer in lieu of consideration at a Closed Meeting (*see* Section 2.5.2.3. of the Manual).

- A MUI must be converted to an investigation before submitting the action memorandum to the Commission.

Considerations:

Please keep the following considerations in mind when deciding whether to seek a formal order:

- Is the formal order action memorandum being provided to the Commission in a timely manner? The memorandum should allow the Commission an opportunity to review the investigation for both policy and resource concerns at a relatively early stage.

- Would the formal order allow the staff to obtain information more efficiently? In addition to efficiently obtaining information, is a subpoena needed to obtain bank or telephone records? Are there persons who will not agree to testify under oath or to provide documents unless subpoenaed?

- Have other interested Divisions and Offices been consulted to identify issues that may arise from potential violations or that may relate to the investigation?

- Such action memoranda are privileged and non-public. Staff should use internal standardized templates, modified to suit the facts and circumstances of the investigation.

#### 2.3.4.1 Supplementing a Formal Order

Once a formal order of investigation has been issued by the Commission, the Division has authority, delegated to it from the Commission, to name staff members as officers empowered to issue subpoenas and administer oaths, among other things. 17 C.F.R. Section 200.30-4(a)(1) and (4). During the course of a formal investigation, the Division may request that the Secretary of the Commission issue a supplemental order to add or remove staff members from the list of officers named in the original formal order. A supervisor at the Assistant Director level or above may authorize the Division's request fore a supplemental order. Assigned staff in the home office should contact the Office of the Secretary directly to request a supplemental order, and assigned staff in the regional offices should contact the administrative assistants in the Office of Chief Counsel.

#### 2.3.4.2 Requests for a Copy of the Formal Order

Basics:

Rule 7(a) of the SEC's Rules Relating to Investigations provides that a person who is compelled or requested to furnish documentary evidence or testimony at a formal investigative proceeding shall, upon request, be shown the Commission's formal order of investigation. However, a copy of the formal order shall not be furnished to that person

for their retention without the express approval of a Division official at the level of an Assistant Director or District Administrator, or higher. 17 C.F.R. Section 203.7(a).

Procedures for Responding to a Request for a Copy of the Formal Order:

When a member of the staff receives a request for a copy of the formal order, staff should keep in mind the following procedures when determining whether the request should be granted:

- The request must be made by a person or counsel for a person who has been asked to furnish documents or testimony in the formal investigation for which the person is requesting a copy of the formal order.

- The request for a copy of the formal order must be in writing. A copy of the formal order may not be provided on the basis of an oral request. Therefore, staff should advise the person to submit their request in writing to the Assistant Director assigned to the investigation.

- The written request for the formal order must include representations to show that approval of the request is "consistent both with the protection of privacy of persons involved in the investigation and with the unimpeded conduct of the investigation." 17 C.F.R. Section 203.7(a). Staff may furnish the following sample representations to be included in the written request:

  *The undersigned represents _____ in the above captioned matter. Pursuant to 17 C.F.R. §203.7 [I/we] hereby request on behalf of [my/our] client[s] to be furnished with a copy of the Commission's Formal Order of Investigation in the above matter. [I/We] warrant that the Formal Order and information contained therein will remain confidential and will not be disseminated to any person or party except [my/our] client[s] for use in connection with [my/our] representation of [him/her/it/them] in this matter.*

- Only an Assistant Director or higher level Division official may approve a written request for a copy of a formal order. There may be circumstances that warrant denial of the request, such as when there is evidence that the requester intends to use the formal order for purposes outside the representation in the matter, or does not intend to keep the formal order confidential.

- Keep in mind that even a request for a copy of the formal order is denied, a requesting person who is compelled or requested to furnish documentary evidence or testimony at a formal investigative proceeding is still entitled to review the formal order without retaining a copy. 17 C.F.R. Section 203.7.

## 2.4 The Wells Process

The Wells Notice:

Rule 5(c) of the SEC's Rules on Informal and Other Procedures states that the staff may advise persons involved in preliminary or formal investigations "of the general nature of the investigation, including the indicated violations as they pertain to them, and the amount of time that may be available for preparing and submitting a statement prior to the presentation of a staff recommendation to the Commission for the commencement of an administrative or injunction proceeding." 17 C.F.R. Section 202.5(c).

This "Wells notice" evolved from recommendations made by an advisory committee chaired by John Wells. It is advisable to refer back to the intent of the original "Wells Release," in making determinations regarding Wells notices. *See* Securities Act of 1933 ("Securities Act") Release No. 5310, "Procedures Relating to the Commencement of Enforcement Proceedings and Termination of Staff Investigations." As the Commission stated in the Wells Release, "The Commission, however, is also conscious of its responsibility to protect the public interest. It cannot place itself in a position where, as a result of the establishment of formal procedural requirements, it would lose its ability to respond to violative activities in a timely fashion."

Providing a Wells Notice:

The objective of the Wells notice is, as the Commission stated in the Wells Release, "… not only to be informed of the findings made by its staff but also, where practicable and appropriate, to have before it the position of persons under investigation at the time it is asked to consider enforcement action."

The Wells notice should tell a person involved in an investigation that 1) the Division is considering recommending or intends to recommend that the Commission file an action or proceeding against them; 2) the potential violations at the heart of the recommendation; and 3) the person may submit arguments or evidence to the Division and the Commission regarding the recommendation and evidence. The staff is required to obtain a Deputy Director's approval before issuing a Wells notice or determining to recommend an enforcement action without issuing a Wells notice.

To determine whether or when to provide a Wells notice consider:

- Whether the investigation is substantially complete as to the recipient of the Wells notice.

- Whether immediate enforcement action is necessary for the protection of investors. If prompt enforcement action is necessary to protect investors, providing a Wells notice and waiting for a submission may not be practical (for example, a recommendation to file an emergency action requesting a temporary restraining order and asset freeze to stop an ongoing fraud). In addition, providing a Wells notice may alert potential

defendants to the possible asset freeze and put at risk the investor funds that the recommendation is intended to protect.

The Content of the Wells Notice:

A Wells notice should be in writing when possible. If a Wells notice is given orally, it should be promptly followed by written confirmation. If the staff intends to provide a written Wells notice, the staff may give advance notice of the intention to the recipient or his counsel by telephone. As in a Wells notice, the substance of a Wells call should follow the guidance below, but the staff also may refer to specific evidence regarding the facts and circumstances which form the basis for the staff's recommendations.

The written Wells notice or written confirmation of an oral Wells notice should:

- identify the specific charges the staff is considering recommending to the Commission;

- accord the recipient of the Wells notice the opportunity to provide a voluntary statement, in writing or on videotape, arguing why the Commission should not bring an action against them or bringing any facts to the Commission's attention in connection with its consideration of this matter;

- set reasonable limitations on the length of any submission made by the recipient (typically, written submissions should be limited to 40 pages, not including exhibits, and video submissions should not exceed 12 minutes), as well as the time period allowed for the recipients to submit a voluntary statement in response to the Wells notice;

- advise that any submission should be addressed to the appropriate Assistant Director;

- inform the recipient that any Wells submission may be used by the Commission in any action or proceeding that it brings and may be discoverable by third parties in accordance with applicable law; and

- attach a copy of the Wells release, Securities Act Release No. 5310.

- attach a copy of the SEC's Form 1662 ("Supplemental Information for Persons Requested to Supply Information Voluntarily or Directed to Supply Information Pursuant to a Commission Subpoena").

Acceptance of a Wells Submission:

As discussed above, a Wells notice informs a recipient that they are entitled to make a voluntary submission to the Commission regarding the Division's proposed

recommendation. However, there are circumstances in which the staff may reject a Wells submission:

- If the Wells submission exceeds the limitations on length specified in the Wells notice, the staff may reject the submission.

- The staff may determine not to grant a recipient's request for an extension of time. Requests for extensions of time should be made in writing, clearly state the basis for the request, and be directed to the appropriate Assistant Director.

- The staff may reject a submission if the person making the submission limits its admissibility under Federal Rule of Evidence 408 or otherwise limits the Commission's ability to use the submission pursuant to Form 1662.

Wells submissions will be provided to the Commission along with any recommendation from the staff for an unsettled action against the recipient of the Wells notice.

The Post-Notice Wells Process:

- Recipients of Wells notices often request to review portions of the staff's investigative file. On a case-by-case basis, it is within the staff's discretion to allow the recipient of the notice to review non-privileged portions of the investigative file, including documents that the recipient likely would receive during discovery if the Commission were to file a recommended action or proceeding. In considering a request for access to the staff's investigative file, the staff should keep in mind:

    - whether access would be a productive way for both the staff and the recipient of the Wells notice to gauge the strength of the evidence that forms the basis for the staff's recommendations;

    - whether the prospective defendant or respondent invoked his Fifth Amendment rights or otherwise refused to testify during the investigation; and

    - the stage of the investigation with regard to other persons or witnesses, including whether certain witnesses have yet to provide testimony.

- Recipients of Wells notices may request meetings with the staff to discuss the substance of the staff's proposed recommendation to the Commission. Assigned staff should consult with supervisors if such a request is made.

- The staff may engage in appropriate settlement discussions with the recipient of the Wells notice. However, the staff may choose to inform the recipient that the staff will not engage in prolonged settlement discussions which would delay timely consideration of the matter by the Commission.

The Commission's Wells Release:

PROCEDURES RELATING TO THE COMMENCEMENT OF ENFORCEMENT PROCEEDINGS AND TERMINATION OF STAFF INVESTIGATIONS

SECURITIES ACT OF 1933, Release No. 5310; SECURITIES EXCHANGE ACT OF 1934, Release No. 9796; INVESTMENT COMPANY ACT OF 1940, Release No. 7390; INVESTMENT ADVISORS ACT OF 1940, Release No. 336

September 27, 1972

The Report of the Advisory Committee on Enforcement Policies and Practices, submitted to the Commission on June 1, 1972, contained several recommendations designed to afford persons under investigation by the Commission an opportunity to present their positions to the Commission prior to the authorization of an enforcement proceeding.[2] These procedural measures, if adopted, would in general require that a prospective defendant or respondent be given notice of the staff's charges and proposed enforcement recommendation and be accorded an opportunity to submit a written statement to the Commission which would accompany the staff recommendation. The objective of the recommended procedures is to place before the Commission prior to the authorization of an enforcement proceeding the contentions of both its staff and the adverse party concerning the facts and circumstances which form the basis for the staff recommendation.[3]

The Commission has given these recommendations careful consideration. While it agrees that the objective is sound, it has concluded that it would not be in the public interest to adopt formal rules for that purpose. Rather, it believes it necessary and proper

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[2] See Report of the Advisory Committee on Enforcement Policies and Practices, June 1, 1972, page 31 et seq.

[3] It should be noted that the obtaining of a written statement from a person under investigation is expressly authorized by Section 20(a) of the Securities Act of 1933 and Section 21(a) of the Securities Exchange Act of 1934. Section 21(a) of the Exchange Act provides as follows:

> "The Commission may, in its discretion, make such investigations as it deems necessary to determine whether any person has violated or is about to violate any provision of this title or any rule or regulation thereunder, and may require or permit any person to file with it a statement in writing, under oath or otherwise as the Commission shall determine, as to all the facts and circumstances concerning the matter to be investigated. . . ."

that the objective be attained, where practicable, on a strictly informal basis in accordance with procedures which are now generally in effect.

The Commission desires not only to be informed of the findings made by its staff but also, where practicable and appropriate, to have before it the position of persons under investigation at the time it is asked to consider enforcement action.

The Commission, however, is also conscious of its responsibility to protect the public interest. It cannot place itself in a position where, as a result of the establishment of formal procedural requirements, it would lose its ability to respond to violative activities in a timely fashion.

The Commission believes that the adoption of formal requirements could seriously limit the scope and timeliness of its possible action and inappropriately inject into actions it brings issues, irrelevant to the merits of such proceedings, with respect to whether or not the defendant or respondent had been afforded an opportunity to be heard prior to the institution of proceedings against him and the nature and extent of such opportunity.

The Commission is often called upon to act under circumstances which require immediate action if the interests of investors or the public interest are to be protected. For example, in one recent case involving the insolvency of a broker-dealer firm, the Commission was successful in obtaining a temporary injunctive decree within 4 hours after the staff had learned of the violative activities. In cases such as that referred to, where prompt action is necessary for the protection of investors, the establishment of fixed time periods, after a case is otherwise ready to be brought, within which proposed defendants or respondents could present their positions would result in delay contrary to the public interest.

The Commission, however, wishes to give public notice of a practice, which it has heretofore followed on request, of permitting persons involved in an investigation to present a statement to it setting forth their interests and position. But the Commission cannot delay taking action which it believes is required pending the receipt of such a submission, and, accordingly, it will be necessary, if the material is to be considered, that it be timely submitted. In determining what course of action to pursue, interested persons may find it helpful to discuss the matter with the staff members conducting the investigation. The staff, in its discretion, may advise prospective defendants or respondents of the general nature of its investigation, including the indicated violations as they pertain to them, and the amount of time that may be available for preparing a submission. The staff must, however, have discretion in this regard in order to protect the public interest and to avoid not only delay, but possible untoward consequences which would obstruct or delay necessary enforcement action.

Where a disagreement exists between the staff and a prospective respondent or defendant as to factual matters, it is likely that this can be resolved in an orderly manner only through litigation. Moreover, the Commission is not in a position to, in effect,

adjudicate issues of fact before the proceeding has been commenced and the evidence placed in the record. In addition, where a proposed administrative proceeding is involved, the Commission wishes to avoid the possible danger of apparent prejudgment involved in considering conflicting contentions, especially as to factual matters, before the case comes to the Commission for decision. Consequently, submissions by prospective defendants or respondents will normally prove most useful in connection with questions of policy, and on occasion, questions of law, bearing upon the question of whether a proceeding should be initiated, together with considerations relevant to a particular prospective defendant or respondent which might not otherwise be brought clearly to the Commission's attention.

Submissions by interested persons should be forwarded to the appropriate Division Director or Regional Administrator with a copy to the staff members conducting the investigation and should be clearly referenced to the specific investigation to which it relates. In the event that a recommendation for enforcement action is presented to the Commission by the staff, any submissions by interested persons will be forwarded to the Commission in conjunction with the staff memorandum.

It is hoped that this release will be useful in encouraging interested persons to make their views known to the Commission and in setting forth the procedures by which that objective can best be achieved.

The Advisory Committee also recommended that the Commission should adopt in the usual case the practice of notifying a person who is the subject of an investigation, and against whom no further action is contemplated, that the staff has concluded its investigation of the matters referred to in the investigative order and has determined that it will not recommend the commencement of an enforcement proceeding against him.[4]

We believe this is a desirable practice and are taking steps to implement it in certain respects. However, we do not believe that we can adopt a rule or procedure under which the Commission in each instance will inform parties when its investigation has been concluded. This is true because it is often difficult to determine whether an investigation has been concluded or merely suspended, and because an investigation believed to have been concluded may be reactivated as a result of unforeseen developments. Under such circumstances, advice that an investigation has been concluded could be misleading to interested persons.

The Commission is instructing its staff that in cases where such action appears appropriate, it may advise a person under inquiry that its formal investigation has been terminated. Such action on the part of the staff will be purely discretionary on its part for the reasons mentioned above. Even if such advice is given, however, it must in no way be construed as indicating that the party has been exonerated or that no action may ultimately result from the staff's investigation of that particular matter. All that such a communication means is that the staff has completed its investigation and that at that time

[4] Report, page 20.

no enforcement action has been recommended to the Commission. The attempted use of such a communication as a purported defense in any action that might subsequently be brought against the party, either civilly or criminally, would be clearly inappropriate and improper since such a communication, at the most, can mean that, as of its date, the staff of the Commission does not regard enforcement action as called for based upon whatever information it then has. Moreover, this conclusion may be based upon various reasons, some of which, such as workload considerations, are clearly irrelevant to the merits of any subsequent action.

By the Commission.

Further Information:

Please consult with the Office of Chief Counsel concerning any questions relating to the Wells process.

## 2.5 Enforcement Recommendations

### 2.5.1 The Action Memo Process

The filing or institution of any enforcement action must be authorized by the Commission. In addition, while the Commission has delegated certain authority to the Division Director or the Secretary, most settlements of previously authorized enforcement actions, as well as certain other aspects of civil litigation, distribution of Fair Funds, and collection of debts, among other things, require Commission authorization. Because obtaining needed authorization before acting is critical, please consult with senior managers, the Division's Office of Chief Counsel, and, if appropriate, the Office of the General Counsel, before taking action to ensure that you seek the required authorization for all aspects of your matter.

Commission authorization is sought by submitting an action memorandum to the Commission that sets forth a Division recommendation and provides a comprehensive explanation of the recommendation's factual and legal foundation. All action memoranda submitted to the Commission must be authorized by the Director or a Deputy Director, with a few exceptions. Formal order action memoranda, memoranda seeking authorization to seek a specific penalty in previously filed civil litigation, and memoranda seeking the termination or discharge of debts may be submitted to the Commission upon the authorization of an Associate Director or Regional Head of Enforcement, provided that they do not present significant issues that merit higher-level authorization. Staff should consult with senior managers to ensure that appropriate authorization within the Division is obtained before submitting any recommendation.

Prior to submitting an action memorandum to the Commission, staff should solicit review and comment from the Division's Office of Chief Counsel, the SEC's Office of the General Counsel, and other interested Divisions or Offices.

### 2.5.2 Commission Authorization

After the Division presents a recommendation to the Commission, the Commission will consider the recommendation and vote on whether to approve or reject it. The Commission's consideration of the recommendation takes place in a closed Commission meeting, by seriatim consideration, or by Duty Officer consideration.

A quorum of three or more Commissioners may approve a recommendation with a majority vote. If fewer than three Commissioners are currently appointed to the Commission, a quorum will consist of the number of Commissioners actually in office. If any Commissioners are *recused* from participating (as opposed to being unavailable to participate), two Commissioners may constitute a quorum. If only one Commissioner is not recused from participating, the matter must be deferred unless there are exigent circumstances, in which case the matter may be considered by the Duty Officer. 17 C.F.R. Section 200.41.

Before any recommendation is considered by the Commission, the staff must identify the counsel representing the subjects of the proposed enforcement action, so that the Commissioners may determine whether they may need to recuse themselves from considering the matter.

#### 2.5.2.1 Closed Meetings

The Commission considers and votes on some of the Division's recommendations in "closed meetings," which are meetings that the Commission, pursuant to exemptions in the Government in the Sunshine Act ("Sunshine Act"), has voted to close to the public. For each matter which will be considered in a closed meeting, the staff prepares a Sunshine Act certification, to be signed by the General Counsel of the Commission, certifying that the matter falls within one of the exemptions provided by Title 5, Section 552 of the United States Code and Title 17, Section 200.402(a) of the Code of Federal Regulations. Generally, recommendations that are eligible to be considered at a closed meeting include recommendations to open a formal investigation; to institute, modify, or settle an enforcement action; to consider an offer of settlement; or to terminate a debt owed by an individual.

At a closed meeting, Division staff orally presents a recommendation to the Commission and answers its questions before the Commission votes on the recommendation. Except in unusual circumstances, the Commissioners receive a copy of the Division's recommendation prior to the closed meeting. Staff should be prepared to answer the questions that are likely to be asked by the Commissioners and should contact the Commissioners' offices prior to the meeting to learn of any particular concerns or questions about the recommendation.

### 2.5.2.2 Seriatim Consideration

If the Chairman or the Duty Officer (*see* Section 2.5.2.3. of the Manual), determines that consideration of a recommendaton at a closed meeting is "unnecessary in light of the nature of the matter, impracticable, or contrary to the requirements of agency business," but that the recommendation should be the subject of a vote by the entire Commission, the recommendation may acted upon separately by each Commissioner in turn – in other words, by seriatim consideration. 17 C.F.R. Section 200.42.

Seriatim consideration is often used when the agenda of a closed meeting is filled or the date of a closed meeting is too distant to meet the timing needs of a particular recommendation. In addition, a recommendation may be circulated seriatim when it is routine or does not qualify under the Sunshine Act for consideration at a closed meeting. Matters that urgently require action before the next available Commission meeting, but raise issues sufficient to warrant consideration by the entire Commission, may, with the consent of the Chairman or Duty Officer, circulate on an expedited basis for rapid seriatim consideration. Staff should consult the Division's Office of Chief Counsel and the Office of the Secretary for the specific procedures required for submitting seriatim items.

Each participating Commissioner will report his or her vote on the recommendation to the Secretary of the Commission, using a seriatim coversheet prepared by the staff and approved by the Secretary. Even if a majority of the Commission has voted in favor of a seriatim recommendation, the matter is not authorized until each Commissioner has either recorded a vote or indicated that he or she is not participating. Any member of the Commission may pull a recommendation from seriatim circulation and instead place it on a closed meeting agenda for further consideration.

### 2.5.2.3 Duty Officer Consideration

The Commission delegates one of its members (other than the Chairman) as the Duty Officer on a rotating basis, empowering the Duty Officer to act, in his or her discretion, on behalf of the entire Commission when urgent action is required before a recommendation can be considered at a closed meeting or by seriatim. 17 C.F.R. Section 200.43. All decisions of the Duty Officer subsequently circulate among the other Commissioners for affirmation.

Generally, requests for Duty Officer consideration should result from an unavoidable and pressing external need. Typically, Duty Officer consideration is sought when the staff has recently become aware of imminent potential harm to investors, and the Division either requires immediate formal order authority to obtain needed records or intends to recommend an emergency enforcement action, such as an immediate trading suspension or a civil action for a temporary restraining order. Duty Officer consideration should, as a general matter, not be sought where an enforcement recommendation presents close legal issues regarding jurisdiction or liability. Additionally, Duty Officer

consideration is generally not an appropriate means to obtain approval of a proposed settlement. Staff should consult with the Office of Chief Counsel and the Office of the Secretary to determine if Duty Officer consideration might be appropriate.

### 2.5.3 Delegations of Commission Authority

The Commission has delegated certain limited aspects of its authority to the various Divisions and Offices, including delegations to the Director of the Division of Enforcement to file subpoena enforcement actions and to the Secretary of the Commission to issue orders instituting or settling certain administrative proceedings. 17 C.F.R. Section 200.30 *et seq.*

Subpoena Enforcement Actions:

If a person or entity refuses to comply with a subpoena issued by the staff pursuant to a formal order of investigation, the Commission may file a subpoena enforcement action in federal district court, seeking an order compelling compliance (*see* Section 21(c) of the Exchange Act). The Commission has delegated the authority to file such an action to the Director of the Division. 17 C.F.R. Section 200.30-4(10).

If, after a reasonable and good faith attempt to resolve disagreements with defense counsel, a civil action is necessary and appropriate to enforce compliance with a subpoena, the staff must obtain the approval of the assigned Associate Director or Regional Head of Enforcement before seeking the Director's authorization to file a subpoena enforcement action. If the Director agrees that subpoena enforcement is appropriate and necessary, the assigned staff should prepare a memorandum to the Director, laying out the basis for the recommended action, and seeking his or her signature authorizing the action.

Follow-on Administrative Proceedings:

The Secretary has delegated authority to issue certain orders in administrative proceedings. 17 C.F.R. Section 200.30-7. Most significantly, the Secretary may issue orders instituting previously authorized ("follow-on") administrative proceedings to determine whether barring a person from association with a broker-dealer or investment adviser is appropriate based on the entry of a civil injunction or criminal conviction against that person. The Secretary may also, pursuant to delegated authority, enter an order imposing a permanent bar in such cases, if the respondent consents. 17 C.F.R. Section 200-30.7(12).

In practical terms, this means that it is not necessary to prepare an action memorandum recommending that the Commission institute an order to impose follow-on administrative relief under Section 15(b) of the Exchange Act or Section 203(f) of the Investment Advisers Act of 1940 ("Advisers Act") if: 1) the Commission previously authorized a "follow-on" administrative proceeding as part of a prior recommendation, and 2) the injunction or criminal conviction has been entered. Further, the Secretary has

delegated authority to institute a settled order if the person consents to the full administrative relief authorized by the Commission (a permanent bar). Because it is critically important to determine that the conditions above have been met and that the order to be issued falls clearly within the Secretary's delegated authority, staff should consult with the Office of Chief Counsel and the Office of the Secretary before submitting an order for issuance pursuant to delegated authority.

## 2.6 Closing an Investigation

### 2.6.1 Policies and Procedures

Basics:

Properly closing an investigation is an important part of managing investigations and making the best use of our resources. Closing investigations where there has been enforcement action is relatively easy; the staff simply makes sure that it has followed through on every step authorized by the Commission. Closing investigations where no enforcement action will be recommended can be a harder judgment call. The staff is encouraged to close an investigation as soon as it becomes apparent that no enforcement action will be recommended. This may mean that every investigative step has not been completed when the closing decision is made. Staff is encouraged to make this decision, however, so that resources can be redirected to investigations that will be more productive.

Generally, factors that should be considered in deciding whether to close an investigation include:

- The seriousness of the potential violations;
- The staff resources available to pursue the investigation;
- The sufficiency of the evidence; and
- The age of the conduct underlying the potential violations.

Considerations:

Once a decision has been made to close an investigation, there are several steps that the staff must take. These steps create the official record and ensure that documents obtained during the investigation are handled properly:

- Check with the Freedom of Information Act ("FOIA") Office. Records that are subject to a request from a member of the public under FOIA cannot be destroyed. If no FOIA issues exist, the staff may prepare the files for disposition. If a FOIA issue exists, the FOIA office will advise the staff on the proper disposition of the case files. For example, the staff may be asked to include records subject to a pending FOIA request in the files going to storage even though the records would otherwise not be retained after the case is closed.

- Prepare a closing recommendation. The closing recommendation is a short memorandum and serves as the basic historical record summarizing what the staff did in the investigation and action.

- Prepare the files for disposition. Remember that electronic records obtained or generated during the investigation will also require proper disposition.

- Prepare and send appropriate termination notices.

Closing investigations that have resulted in an enforcement action have special issues. An investigation cannot be closed until all enforcement actions in the case are complete. This requires (1) a final judgment or Commission order and (2) that all ordered monetary relief is accounted for, meaning:

- All disgorgement and civil penalties have been paid in full or the Commission has authorized the staff to terminate collection of any unpaid amounts;

- All funds collected have either been distributed to investors or paid into the Treasury; and

- All money has been properly recorded.

- Further, an investigation cannot be closed if any debts of a defendant/respondent are the subject of collection activity by the Commission or on the Commission's behalf (e.g., by the Department of the Treasury's Financial Management Service or the Department of Justice), or if any funds are being held pending final distribution.

Further Information:

Staff should contact the Office of Chief Counsel with questions about closing a case.

### 2.6.2 Termination Notices

Basics:

The Division's policy is to notify individuals and entities at the earliest opportunity when the staff has determined not to recommend an enforcement action against them to the Commission. This notification takes the form of a termination letter. The staff may send termination letters to individuals or entities before the investigation is closed and before a determination has been made as to every potential defendant or respondent. Termination letters should be sent regardless of whether the investigation was pursuant to a formal order.

A termination letter must be sent to anyone who:

- Is identified in the caption of the formal order;
- Submitted or was solicited to submit a Wells submission;
- Asks for such a notice (assuming the staff has decided that no enforcement recommendation will be recommended against that person or entity); or
- Reasonably believes that the staff was considering recommending an enforcement action against them.

If the staff decides against sending a termination letter to persons or entities that fall into any of the above categories, an Associate Director or Regional Head of Enforcement must be notified and approve of the decision. The termination letter should be signed by an Assistant Director or above and a copy of the Commission's Wells Release (Securities Act Release No. 5310), which authorized termination notices, should be attached to each termination letter. As noted in the Commission's Wells Release, the provision of a termination notice "must in no way be construed as indicating that the party has been exonerated or that no action may ultimately result from the staff's investigation of that particular matter. All that such a communication means is that the staff has completed its investigation and that at that time no enforcement action has been recommended to the Commission."

Considerations:

Staff should also consider sending termination letters to companies who provided information concerning their securities in connection with insider trading investigations.

Sample Termination Letter:

[Date]

RE: In the Matter of

Dear :

This investigation has been completed as to [name of related party receiving notice], against whom we do not intend to recommend any enforcement action by the Commission. We are providing this information under the guidelines in the final paragraph of Securities Act Release No. 5310 (copy attached).

Very truly yours,

Assistant Director

## 3. A Guide to Investigative Practices

### 3.1 Special Considerations

#### 3.1.1 External Communications Between Senior Enforcement Officials and Persons Outside the SEC Who Are Involved in Investigations

Introduction

The purpose of these best practices is to ensure that external communications between senior enforcement officials (at the Associate Director level and above) and persons outside the SEC are handled with the appropriate care, sensitivity and transparency. These best practices concern only external communications that are: 1) material; 2) relate to ongoing, active investigations; and 3) occur between senior enforcement officials and persons outside the SEC who are involved with investigations (other than persons at agencies or organizations with which the SEC cooperates).

Staff at all levels of the Division of Enforcement play an essential role in seeking and receiving the information required to discharge their investigative and decision-making responsibilities, and it is important that outside persons involved in investigations feel that they may contact the staff in the Division without hesitation, including senior officials. In fact, a senior official may obtain particularly valuable information through material external communications. To present one consistent Division position to persons involved in investigations, and continue to maintain the Division's impartiality and history of handling investigations with integrity, senior officials should take into consideration the best practices described below. Underlying these best practices is the recognition of the importance of the investigative team's responsibility to gather evidence, raise questions, and manage relationships with outside persons during an investigation. The best practices reflect the practical realities of the teamwork required by all staff involved in an investigation (from staff attorney to the most senior official), while taking into account the flexibility necessary to engage in communications in situations and under circumstances that may present unforeseen variables.

Best Practices

These best practices should be applied to all situations in which senior officials engage in material communications with persons outside the SEC relating to ongoing, active investigations:

- Generally, senior officials are encouraged to include other staff members on the investigative team when engaging in material external communications, and should try to avoid initiating communications without the knowledge or participation of at least one of the other staff members. However, "participation" could include either having another staff member present during the communications, or having a staff member involved in preparing the senior official for the communications. For example, if the investigative team believes

that a communication could be more productive as a one-on-one communication between the senior official and the outside person, members of the team could participate by discussing the case with the senior official prior to the meeting, or assisting in preparing talking points for the senior official to use during the communication.

- Although senior officials are encouraged to include other staff members on the investigative team when engaging in a communication, there are circumstances in which none of the staff members are available to participate when an outside person initiates a communication. Under those circumstances, the senior official may need to balance several factors to determine whether to entertain the communication without the participation of other staff members, including:

    - Whether the senior official is familiar with the context and facts that are the subject of the communication;

    - Whether the investigative team is aware that the outside person planned to initiate a communication with the senior official;

    - Whether the outside person had previously discussed the matter with others on the investigative team (and how the team responded);

    - Whether the senior official was briefed by the investigative team regarding the communication; and

    - Whether the communication involves a matter of urgency, a routine issue, or a more complex situation in which the outside person is seeking an agreement or representation regarding a material aspect of the investigation.

- If a senior official entertains a communication without the participation or presence of other staff members, then the senior official should indicate to the outside person that the senior official will be informing other members of the investigative team of the fact of the communication, along with any pertinent details, for their information and consideration, and should consider:

    - Indicating to the outside person that the fact that the senior official is entertaining the communication does not imply acquiescence or agreement; and

    - Indicating to the outside person that the senior official is not in a position to reach an agreement or make a representation without reviewing the circumstances with other investigative team members (however, the senior official need not avoid reaching an agreement or making representations if any of the staff prepared the senior official for the communication in anticipation that agreements or representations might be discussed).

- Within a reasonable amount of time, the senior official should document material external communications related to the investigation involving, but not limited to, potential settlements, strength of the evidence, and charging decisions. The official may take contemporaneous notes of the communication, send an email to any of the assigned staff, prepare a memo to the file, or orally report details to any of the assigned staff (who may then take notes or prepare a memo to the file).

- The senior official should at all times keep in mind the need to preserve the impartiality of the Division in conducting its fact-finding and information-gathering functions. Propriety, fairness, and objectivity in investigations are of the utmost importance, and the investigative team cannot carry out its responsibilities appropriately unless these principles are strictly maintained. The senior official should be particularly sensitive that an external communication may appear to be or has the potential to be an attempt to supersede the investigative team's judgment and experience.

Considerations:

- There may be circumstances in which a senior official and an outside person find it necessary to discuss the professionalism of assigned staff or allegations regarding questionable conduct by the assigned staff. Even if the communication could be considered a material communication about the investigation itself, the senior official may choose not to inform any of the assigned staff about the communication. The senior official, however, should be sensitive to the possibility that allegations about questionable conduct may serve as a pretext to complain about minor events or annoyances during the investigative process, to gain an advantage in the investigation or to undermine the progress of the investigation. Depending on the apparent motivation of the communication, the senior official should consider whether to inform the staff of the communication, following the best practices above.

- If any of the investigative team members learn that a person outside the SEC might contact a senior official, the staff member should alert the senior official as soon as possible and provide all pertinent details concerning the anticipated subject matter of the communication.

- In addition to the best practices above and the typical considerations that apply when an SEC employee communicates with someone outside the agency involved in an enforcement investigation, senior officials and other investigative team members should recognize the discretion and judgment inherent in balancing all the circumstances of a potential communication with outside persons, including:

    - the time, place, and context of the communication;

- the availability and accessibility of any of the assigned staff to participate in the communication;

- the expected or anticipated subject matter of the communication ;

- the priority, phase and sensitivity of the investigation, including the status of the Wells process or any pending settlement discussions;

- the complexity and circumstances of the suspected securities law violations at issue;

- the need to further the Commission's interests in the investigation and in the protection of investors;

- the level of cooperation of witnesses and their counsel; and

- the existence of criminal interest.

Further Information:

For questions concerning the applicability of these best practices, please contact the Office of Chief Counsel.

### 3.1.2 Statutes of Limitations and Tolling Agreements

Basics:

- Section 2462 of Title 28 of the United States Code states that "[e]xcept as otherwise provided by Act of Congress, an action, suit or proceeding for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise, shall not be entertained unless commenced within five years from the date when the claim first accrued if, within the same period, the offender or the property is found within the United States in order that proper service may be made thereon." The statute of limitations is an affirmative defense that is waived if it is not raised in timely fashion. *See* Canady v. SEC, 230 F.3d 362, 363 (D.C. Cir. 2000).

- If the assigned staff investigating potential violations of the federal securities laws believes that any of the suspect conduct may be outside the five-year limitations period before the SEC would be able to file or institute an enforcement action, the staff may ask the potential defendant or respondent to sign a "tolling agreement." Such requests are often made in the course of settlement negotiations to allow time for sharing of information in furtherance of reaching a settlement. By signing a tolling agreement, the potential defendant or respondent agrees not to assert a statute of limitations defense in the enforcement action for a specified time period. A tolling agreement must be signed by staff at the Assistant Director level or above.

Sample Language:

The following is an example of a tolling agreement:

TOLLING AGREEMENT

WHEREAS, the Division of Enforcement ("Division") of the United States Securities and Exchange Commission ("Commission") has notified [Respondent/Defendant], through [his/her/its] counsel, that the Division is conducting an investigation entitled In the Matter of [ ] (the "investigation") to determine whether there have been violations of certain provisions of the federal securities laws;

ACCORDINGLY, IT IS HEREBY AGREED by and between the parties that:

1. the running of any statute of limitations applicable to any action or proceeding against [Respondent/Defendant] authorized, instituted, or brought by or on behalf of the Commission or to which the Commission is a party arising out of the investigation ("any proceeding"), including any sanctions or relief that may be imposed therein, is tolled and suspended for the period beginning on [DATE] through [DATE] (the "tolling period");

2. [Respondent/Defendant] and any of [his/her/its] agents or attorneys shall not include the tolling period in the calculation of the running of any statute of limitations or for any other time-related defense applicable to any proceeding, including any sanctions or relief that may be imposed therein, in asserting or relying upon any such time-related defense;

3. nothing in this agreement shall affect any applicable statute of limitations defense or any other time-related defense that may be available to [Respondent/defendant] before the commencement of the tolling period or be construed to revive any proceeding that may be barred by any applicable statute of limitations or any other time-related defense before the commencement of the tolling period;

4. the running of any statute of limitations applicable to any proceeding shall commence again after the end of the tolling period, unless there is an extension of the tolling period executed in writing by and on behalf of the parties hereto; and

5. nothing in this agreement shall be construed as an admission by the Commission or Division relating to the applicability of any statute of limitations to any proceeding, including any sanctions or relief that may be imposed therein, or to the length of any limitations period that may apply, or to the applicability of any other time-related defense.

This instrument contains the entire agreement of the parties and may not be changed orally, but only by an agreement in writing.

SECURITIES AND EXCHANGE COMMISSION
DIVISION OF ENFORCEMENT

By: _____ Date: _____
[Name]
Assistant Director

[INDIVIDUAL RESPONDENT/DEFENDANT]

_____ Date: _____

[CORPORATE RESPONDENT/DEFENDANT

By: _____ Date: _____

Approved as to Form:

, Esq.
[Law Firm Name]

Counsel to [Respondent\Defendant]

Date:

Considerations:

- Consider the statute of limitations issue early in the investigation.

- Take into account the amount of time needed for third parties to complete Wells submissions, for staff to prepare recommendations to the Commission, for interested Divisions and Offices at the SEC to review recommendations, and for the Commission to consider the recommendation.

- Try to avoid multiple requests for tolling agreements by asking for a suitable period of time, keeping in mind that it is ultimately more efficient to overestimate

rather than underestimate the time need to complete the investigation and recommendation to the Commission.

- Section 2462 of Title 28 of the United States Code sets forth a five year statute of limitations, but certain conduct or circumstances may have tolled the statute, depending on the common law developed in a particular jurisdiction. In such situations, please contact a member of the Division's trial unit or the Office of Chief Counsel for further information.

- Keep in mind that certain claims are not subject to the five-year statute of limitations under Section 2462, including claims for injunctive relief and disgorgement.

### 3.1.3 Investigations During Ongoing SEC Litigation

Basics:

The Division may continue to investigate and issue investigative subpoenas pursuant to a formal order of investigation while simultaneously litigating a related civil action if there is an independent, good-faith basis for the continued investigation. An independent, good-faith basis may include the possible involvement of additional persons or entities in the violations alleged in the complaint, or additional potential violations by one or more of the defendants in the litigation.

Considerations:

While the SEC has broad investigative powers, Division staff should exercise judgment when deciding whether to continue investigating while litigating a related case. The staff should review and consider the following:

- In assessing whether to issue subpoenas, the staff should consider all relevant facts and circumstances, including the degree of factual and legal overlap, the prior course of the litigation and investigation, the likely response of defense counsel, and the likely views of the particular judge assigned to the case.

- If the staff obtains testimony or documents in the investigation that are properly discoverable in the litigation, the SEC must produce them in the litigation in accordance with the Federal Rules of Civil Procedure.

- Although there is some case law to support the practice, staff should not use investigative subpoenas solely to conduct discovery with respect to claims alleged in the pending complaint. A court might conclude that the use of investigative subpoenas to conduct discovery is a misuse of the SEC's investigative powers and circumvents the court's authority and the limits on discovery in the Federal Rules of Civil Procedure.

In addition, there are special considerations and restrictions on continuing an investigation following the institution of an administrative proceeding ("AP"):

- In the AP context, continuing investigations are subject to Rule 230(g) of the SEC's Rules of Practice, which requires the Division to inform the hearing officer and each party promptly if the staff issues any new subpoenas under the same formal order. The rule also directs the hearing officer "to order such steps as [are] necessary and appropriate" to assure that the subpoenas are not issued "for the purpose of obtaining evidence relevant to the proceedings." The hearing officer must ensure that any relevant documents obtained through the use of such subpoenas are produced to each respondent "on a timely basis." 17 C.F.R. Section 201.230(g).

Further Information:

Before continuing an investigation while there is related pending litigation, or if the staff is going to recommend to the Commission that a civil action be filed and that a formal order be obtained to investigate, the staff should discuss the issue with trial counsel and should revisit the issue whenever contemplating the service of investigative subpoenas that could be seen as relating to pending litigation.

### 3.1.4. Parallel Investigations and the State Actor Doctrine

Basics of the State Actor Doctrine and When It Applies:

The State Actor Doctrine may be implicated when action by a private entity is fairly attributable to a government entity. The action may be fairly attributable if there is a sufficiently close nexus between the state, or government entity, and the challenged action of a private entity.

The State Actor Doctrine applies to a wide variety of private actions in which government is in some way concerned. It has been analyzed under a two-prong test, either of which can result in a finding of state action:

- Under the "joint action" prong, private entities engage in state action when they are willful participants in joint action with state officials.

- Under the "government compulsion" prong, coercive influence or significant encouragement by the state can convert private conduct into state action.

After a witness asserts the Fifth Amendment privilege during investigative testimony and declines to respond to potentially incriminating questions, the issue may arise if the same witness is then summoned to testify about the same or related conduct by a private entity. When providing testimony to a private entity, the right to assert the Fifth Amendment may not be available to the witness as a practical matter, or its

assertion may result in consequences other than the ability to draw an adverse inference at trial.

Basic Guidelines:

When staff is aware that a private entity is investigating conduct that is the same or related to the conduct involved in the staff's investigation, staff should keep the following guidelines in mind:

- In fact and appearance, the SEC and the private entity's investigations should be parallel and should not be conducted jointly. Staff should make investigative decisions independent of any parallel investigation that is being conducted by a private entity.

- Do not take any investigative step principally for the benefit of the private entity's investigation or suggest investigative steps to the private entity.

- In SEC investigations in which a witness has asserted or indicated an intention to assert the Fifth Amendment in testimony, do not suggest any line of questioning to the private entity conducting a parallel investigation, and do not provide to the private entity any document or other evidence for use in questioning a witness other than pursuant to an approved access request.

Further Information:

Please consult with OCC staff concerning any questions relating to the State Actor Doctrine.

### 3.2 Documents and Other Materials

#### 3.2.1 Privileges and Privacy Acts

In connection with any request for document production, you must comply with the Privacy Act of 1974 ("Privacy Act"), the Right to Financial Privacy Act of 1978 ("RFPA"), and the Electronic Communications Privacy Act of 1986 ("ECPA") and the rules regarding the assertion of privileges, contacting witness's counsel, parallel proceedings, and ongoing litigation. Those rules and statutes are discussed in Section 4.

#### 3.2.2 **Bluesheets**

Basics:

- Bluesheeting is the process by which the SEC requests and obtains trading data from the broker/dealer community. Member firms are required to provide trading information pursuant to Section 17(a) of the Exchange Act and Rule 17a-25

thereunder. Although the process is now handled electronically through the SEC's Bluesheet application, the name derives from the fact that blue paper was once used to make such requests.

- Bluesheet data provides information identifying the account holder for whom specific trades were executed and indicates whether the transaction was a buy or a sell and long or short, among other data elements. The data also identifies proprietary and customer trades executed on all domestic or foreign markets, all "in-house cross" transactions, transactions cleared for introducing brokers, and prime broker transactions.
- It may be appropriate to obtain and review Bluesheet data in a variety of investigations, but it is typically obtained in matters involving possible insider trading or market manipulation violations.

Considerations and Mechanics:

- Prior to requesting bluesheet data, the assigned staff must identify which securities they have an interest in reviewing (equities, options, etc.). Staff must also determine the period of review in which they would like to obtain data. Once these decisions are made, the assigned staff should use the Bluesheet application to obtain Equity Cleared Reports and/or Option Cleared Reports to identify which broker/dealers traded the security at issue.
- Equity and Options Cleared Reports provide essential information such as the clearing firm that reported the trades, volume at each firm, and number of transactions on a daily or specified period. The information can be sorted on a volume basis which allows the staff to quickly determine the largest participants in the marketplace.
    - In a takeover situation, consider organizing the data according to buy volume.
    - If there is suspicious trading before bad news, such as a poor earnings report, it may be appropriate to sort the data by sell volume.

Further Information:

- Questions regarding the Bluesheeting process may be directed to the Division's Office of Market Surveillance.

### 3.2.3 Voluntary Document Requests

Basics:

During an informal inquiry and subsequent informal investigation, the staff may request the voluntary production of documents. The staff also may request the voluntary creation of documents, such as chronologies of events. In an informal inquiry or investigation, the staff can also request that witnesses agree to voluntary interviews and

testimony. It cannot issue subpoenas prior to the Commission's issuance of a Formal Order of Investigation.

When the staff begins an informal inquiry, voluntary document requests are a principal means of gathering documents, data, and other information. Often the fruits of these requests will help the staff assess the merits of an investigation at its earliest stages before the staff opens an informal investigation or requests that the Commission issue a formal order of investigation.

Considerations:

- Many issuers, individuals, and other third parties are willing to provide significant materials to the staff voluntarily, without the provision of a subpoena. And, as discussed in Section 3.2.4 below, regulated entities are required to produce certain records without a subpoena.
- Staff can consider, on a case by case basis, whether and how a voluntary document request as opposed to a subpoena may affect a witness's diligence in his or her search for documents and the witness's responsiveness.
- Staff should also keep in mind that a subpoena is required in some situations, such as when seeking certain information covered by the Electronic Communications Privacy Act.

#### 3.2.3.1 Forms 1661 and 1662

When requesting documents or information other than pursuant to a subpoena, the staff provides all regulated persons or entities with a copy of Form SEC 1661 (entitled "Supplementary Information for Regulated Entities Directed to Supply Information Other Than Pursuant to a Commission Subpoena").

When requesting documents or information (including informal interviews, voluntary or subpoenaed document productions, and testimony) from any witness, the staff provides the witness with a copy of Form SEC 1662 (entitled "Supplemental Information for Persons Requested to Supply Information Voluntarily or Directed to Supply Information Pursuant to a Commission Subpoena").

The Supplemental Information Forms provide information on the following topics:

- False Statements and Documents
- Fifth Amendment
- Right to Counsel
- Going Off the Record
- Consulting with Counsel
- Transcript Availability
- Perjury
- Wells Procedures

- Confidential Treatment Pursuant to the Freedom of Information Act
- Privacy Act Notices:
    - Authority Pursuant to Which Information is Being Solicited
    - Effect of Not Supplying Information
    - Principal Uses of Information
    - Routine Uses of Information

### 3.2.4 Document Requests to Regulated Entities

Basics:

- The staff may request information from regulated entities, such as registered investment advisers and broker-dealers. Pursuant to Sections 17(a) and (b) of the Exchange Act and Section 204 of the Advisers Act and the rules thereunder, regulated entities *must* provide certain information to the staff even without a subpoena.
- Records from regulated entities – especially broker-dealers, transfer agents, and investment advisers – are often essential cornerstones of an investigation. Because regulated entities must produce certain records without a subpoena, the staff can often obtain documents, such as brokerage account statements or account opening documents, which might otherwise require a subpoena to obtain from an individual.

Considerations:

- For reasons of efficiency and strategy, consider what types of records to obtain from a regulated entity. For example, in addition to customer account statements, a broker-dealer will have documents such as order tickets, order confirmations, trading blotters and transfer records.
- Some regulated entities have specific policies regarding whether (and, if so, when) to notify a client or customer that the staff has requested documents related to their account. Even if there is no formal policy in place, the customer or client might be provided some informal notice. Depending on the conduct, potential for investor harm, or other circumstances, consider requesting that a firm not disclose the request for documents, at least for a certain limited period of time.

Further Information:

- Please see Sections 2.2.2.1 and 4.7 of the Manual for information relating to Bank Secrecy Act materials.

- For additional information on documents that may be requested from broker-dealers, and what information such documents can provide, contact the Division's Office of Market Surveillance.

### 3.2.5 Document requests to the News Media

Basics:

The “Policy statement of the Securities and Exchange Commission concerning subpoenas to members of the news media” can be found in Title 17, Section 202.10 of the Code of Federal Regulations.

Text of the Policy Statement:

Freedom of the press is of vital importance to the mission of the Securities and Exchange Commission. Effective journalism complements the Commission's efforts to ensure that investors receive the full and fair disclosure that the law requires, and that they deserve. Diligent reporting is an essential means of bringing securities law violations to light and ultimately helps to deter illegal conduct. In this *Policy Statement the Commission sets forth guidelines for the agency's professional staff* to ensure that vigorous enforcement of the federal securities laws is conducted completely consistently with the principles of the First Amendment's guarantee of freedom of the press, and specifically to avoid the issuance of subpoenas to members of the media that might impair the news gathering and reporting functions. These guidelines shall be adhered to by all members of the staff in all cases:

(a) In determining whether to issue a subpoena to a member of the news media, the approach in every case must be to strike the proper balance between the public's interest in the free dissemination of ideas and information and the public's interest in effective enforcement of the federal securities laws.

(b) When the staff investigating a matter determines that a member of the news media may have information relevant to the investigation, the staff should:

> (1) Determine whether the information might be obtainable from alternative non-media sources.
>
> (2) Make all reasonable efforts to obtain that information from those alternative sources. Whether all reasonable efforts have been made will depend on the particular circumstances of the investigation, including whether there is an immediate need to preserve assets or protect investors from an ongoing fraud.
>
> (3) Determine whether the information is essential to successful completion of the investigation.

(c) If the information cannot reasonably be obtained from alternative sources and the information is essential to the investigation, then the staff, after seeking approval from the responsible Regional Director, District Administrator, or Associate Director, should contact legal counsel for the member of the news media. Staff should contact a member of the news media directly only if the member is not represented by legal counsel. The

purpose of this contact is to explore whether the member may have information essential to the investigation, and to determine the interests of the media with respect to the information. If the nature of the investigation permits, the staff should make clear what its needs are as well as its willingness to respond to particular problems of the media. The staff should consult with the Commission's Office of Public Affairs, as appropriate.

(d) The staff should negotiate with news media members or their counsel, consistently with this Policy Statement, to obtain the essential information through informal channels, avoiding the issuance of a subpoena, if the responsible Regional Director, District Administrator, or Associate Director determines that such negotiations would not substantially impair the integrity of the investigation. Depending on the circumstances of the investigation, informal channels may include voluntary production, informal interviews, or written summaries.

(e) If negotiations are not successful in achieving a resolution that accommodates the Commission's interest in the information and the media's interests without issuing a subpoena, the staff investigating the matter should then consider whether to seek the issuance of a subpoena for the information. The following principles should guide the determination of whether a subpoena to a member of the news media should be issued:

> (1) There should be reasonable grounds to believe that the information sought is essential to successful completion of the investigation. The subpoena should not be used to obtain peripheral or nonessential information.
>
> (2) The staff should have exhausted all reasonable alternative means of obtaining the information from non-media sources. Whether all reasonable efforts have been made to obtain the information from alternative sources will depend on the particular circumstances of the investigation, including whether there is an immediate need to preserve assets or protect investors from an ongoing fraud.

(f) If there are reasonable grounds to believe the information sought is essential to the investigation, all reasonable alternative means of obtaining it have been exhausted, and all efforts at negotiation have failed, then the staff investigating the matter shall seek authorization for the subpoena from the Director of the Division of Enforcement. No subpoena shall be issued unless the Director, in consultation with the General Counsel, has authorized its issuance.

(g) In the event the Director of the Division of Enforcement, after consultation with the General Counsel, authorizes the issuance of a subpoena, notice shall immediately be provided to the Chairman of the Commission.

(h) Counsel (or the member of the news media, if not represented by counsel) shall be given reasonable and timely notice of the determination of the Director of the Division of Enforcement to authorize the subpoena and the Director's intention to issue it.

(i) Subpoenas should be negotiated with counsel for the member of the news media to narrowly tailor the request for only essential information. In negotiations with counsel, the staff should attempt to accommodate the interests of the Commission in the information with the interests of the media.

(j) Subpoenas should, wherever possible, be directed at material information regarding a limited subject matter, should cover a reasonably limited period of time, and should avoid requiring production of a large volume of unpublished material. They should give reasonable and timely notice of their demand for documents.

(k) In the absence of special circumstances, subpoenas to members of the news media should be limited to the verification of published information and to surrounding circumstances relating to the accuracy of published information.

(l) Because the intent of this policy statement is to protect freedom of the press, news gathering functions, and news media sources, this policy statement does not apply to demands for purely commercial or financial information unrelated to the news gathering function.

(m) Failure to follow this policy may constitute grounds for appropriate disciplinary action. The principles set forth in this statement are not intended to create or recognize any legally enforceable rights in any person.

### 3.2.6 Subpoenas for Documents

Basics:

The Commission, or the staff it designates as officers in a formal order of investigation, may issue subpoenas for documents or witnesses, pursuant to Section 19(c) of the Securities Act, Section 21(b) of the Exchange Act, Section 209(b) of the Advisers Act, and Section 42(b) of the Investment Company Act. The Commission or its designated officers may require the production of any records deemed relevant or material to the inquiry and may require their production from any place in the United States.

- To issue a subpoena for documents, the staff must be named as an officer for purposes of an investigation in the Commission's formal order of investigation. Once the Commission has issued a formal order of investigation, the staff named as officers in the order may issue subpoenas.
- Some documents cannot be obtained without issuing a subpoena, such as records from telephone companies or financial institutions.
- A subpoena for documents should be accompanied by a Form 1662 (and a Form 1661 if issued to a regulated entity).
- Rule 7(a) of the SEC's Rules Relating to Investigations provides that any person who is compelled or required to furnish documents or testimony in a formal investigation

shall, upon request, be shown the formal order of investigation. Such a person may also obtain a copy of the formal order by submitting a written request to the Assistant Director supervising the investigation. *See* 17 C.F.R. Section 201.7(a).

- A subpoena for documents should include an attachment to the subpoena listing the documents requested (generally by category or type of document).

Further Information:

- Subpoenas to financial institutions such as banks and credit card issuers are subject to the Right to Financial Privacy Act. For more information on this Act, please see Section 4.5 of the Manual.
- For procedures on granting a request for a copy of the formal order, see Section 2.4.3 of the Manual.
- For more information about Forms 1661 and 1662, see Section 3.2.3.1 of the Manual.

### 3.2.6.1 Service of Subpoenas

Under Rule 8 of the SEC's Rules Relating to Investigations (17 C.F.R. Section 203.8), service of subpoenas issued in formal investigative proceedings shall be effected in the manner prescribed by Rule 232(c) of the SEC's Rules of Practice (17 C.F.R. Section 201.232(c)). Rule 232(c), in turn, states that service shall be made pursuant to the provisions of Rule 150(b) through (d) of the SEC's Rules of Practice (17 C.F.R. Sections 201.150(b) through (d)).

Rule 150 provides that service of subpoenas may be effected:

(b) Upon a person represented by counsel. Whenever service is required to be made upon a person represented by counsel who has filed a notice of appearance pursuant to Sec. 201.102, service shall be made pursuant to paragraph (c) of this section upon counsel, unless service upon the person represented is ordered by the Commission or the hearing officer.

(c) How made. Service shall be made by delivering a copy of the filing. Delivery means:

(1) Personal service--handing a copy to the person required to be served; or leaving a copy at the person's office with a clerk or other person in charge thereof, or, if there is no one in charge, leaving it in a conspicuous place therein; or, if the office is closed or the person to be served has no office, leaving it at the person's dwelling house or usual place of abode with some person of suitable age and discretion then residing therein;

(2) Mailing the papers through the U.S. Postal Service by first class, registered, or certified mail or Express Mail delivery addressed to the person;

(3) Sending the papers through a commercial courier service or express delivery service; or

(4) Transmitting the papers by facsimile transmission where the following conditions are met:

(i) The persons so serving each other have provided the Commission and the parties with notice of the facsimile machine telephone number to be used and the hours of facsimile machine operation;

(ii) The transmission is made at such a time that it is received during the Commission's business hours as defined in Sec. 201.104; and

(iii) The sender of the transmission previously has not been served in accordance with Sec. 201.150 with a written notice from the recipient of the transmission declining service by facsimile transmission.

(d) When service is complete. Personal service, service by U.S. Postal Service Express Mail or service by a commercial courier or express delivery service is complete upon delivery. Service by mail is complete upon mailing. Service by facsimile is complete upon confirmation of transmission by delivery of a manually signed receipt.

#### 3.2.6.2 Form of Production

Basics:

- The following guidelines for production should be set out in the subpoena or in the cover letter accompanying the subpoena.

- Generally, all documents described in the attachment to the subpoena should be produced by the date listed on the subpoena. The documents should also be produced to the particular staff member identified in the subpoena.

- The subpoenaed entity or individual is required to produce all subpoenaed items that are in its possession, custody or control. This includes items under the subpoenaed entity or individual's control or custody, but that are not in its immediate possession.

- The staff is encouraged to request document production in electronic format, in an SEC preferred format, and to include OCR text. Electronic production is preferable, especially large productions from entities, because it is less costly, the information may be stored more efficiently, it may allow the staff to search for specific terms, and it may provide the ability to tag and review data more easily. Requesting the production in an SEC preferred format and to include OCR text also reduces costs.

- In an electronic production, the subpoenaed entity or individual must maintain the originals of all documents responsive to the subpoena in the event production of the original documents is required at a later date.

- If the subpoenaed entity or individual produces documents in electronic format, the subpoenaed entity or individual should advise the staff, as soon as possible, of the size of the document production, the software used to store the document, and the medium of production.

- The staff may allow the subpoenaed entity or individual to produce documents in hard paper copies. In the event that the subpoenaed entity or individual produces documents in hard paper copies, the subpoenaed entity or individual must maintain the originals of all documents responsive to the subpoena in the event production of the original documents is required at a later date.

- If copies of a document differ in any way, they are to be treated as separate documents and the subpoenaed entity or individual must produce each copy. For example, if the subpoenaed entity or individual has two copies of the same letter, but only one of them is marked with handwritten notes, the subpoenaed entity or individual must send both the clean copy and the copy with notes.

- The subpoenaed entity or individual should produce hard copy and electronic documents in a unitized manner, e.g., delineated with staples or paper clips to identify the document boundaries.

- The subpoenaed entity or individual should enclose a list briefly describing each item it has sent. The list should include the paragraph(s) in the subpoena attachment to which each item responds.

- The subpoenaed entity or individual should also include a cover letter stating whether it believes it has met its obligations under the subpoena by searching carefully and thoroughly for all documents or materials required by the subpoena, and by producing all of the required documents and materials.

- The term “document” in the context of a production responsive to a subpoena includes, but is not limited to, any written, printed, or typed matter in the possession, custody or control of the subpoenaed entity or individual including, but not limited to all drafts and copies bearing notations or marks not found in the original, letters and correspondence, interoffice communications, slips, tickets, records, worksheets, financial records, accounting documents, bookkeeping documents, memoranda, reports, manuals, telephone logs, telegrams, facsimiles, messages of any type, telephone messages, voice mails, tape recordings, notices, instructions, minutes, summaries, notes of meetings, file folder markings, and any other organizational indicia, purchase orders, information recorded by photographic process, including microfilm and microfiche, computer printouts, spreadsheets, and other information filed or stored in computers on magnetic or optical media, on back-up tapes or recordings, or otherwise, which can be retrieved, obtained, manipulated, or translated.

- The subpoenaed entity or individual must produce all of the materials described in the subpoena. If, for any reason, the subpoenaed entity or individual does not produce something required by the subpoena, the subpoenaed entity or individual should submit a list of what it is not producing. The list should describe each item separately, noting: its author(s); its date; its subject matter; the name of the person who has the item now, or the last person known to have it; the names of everyone who ever had the item or a copy of it, and the names of everyone who was told the item's contents; and the reason the subpoenaed entity or individual did not produce the item.

- If the subpoenaed entity or individual withholds an item based on a claim of privilege, the list of withheld items should specify the privilege claimed. If the subpoenaed entity or individual withholds anything on the basis of a claim of attorney-client privilege or attorney work product protection, the subpoenaed entity or individual should identify the attorney and client involved**.**

- If any documents responsive to the subpoena no longer exist because they have been lost, discarded, or otherwise destroyed, the subpoenaed entity or individual should identify such documents and give the date on which they were lost, discarded or destroyed.

- Many larger accounting firms maintain and create their workpapers electronically. Electronic workpapers are often a rich source of metadata and may be easier to navigate than hard copies. Firms may raise concerns about producing electronic workpapers and other audit documents, citing to intellectual property rights in what they view as proprietary programs. The staff does not necessarily agree with the concerns but as an accommodation, may consider alternative approaches such as Web-based production and production on a dedicated laptop computer. These requests may be evaluated on a case-by-case basis to determine whether an alternative approach is appropriate in your investigation.

<u>Further Information</u>:

- Please refer any questions about the form of production to the Trial Unit.

- For more information on privilege logs, see Section 3.2.6.2.4 of the Manual.

- For information on the format for electronic production, see Section 3.2.6.2.3 of the Manual.

- For information on certifications of completeness of production, see Section 3.2.6.2.6 of the Manual.

- For more information about when and how to request electronic workpapers, please contact the Chief Accountant, Division of Enforcement.

#### 3.2.6.2.1 Accepting Production of Copies

Basics:

The staff may allow a subpoenaed entity or individual to produce photocopies of the original documents required by a subpoena. Acceptable productions of photocopied documents should follow these guidelines:

- The copies must be identical to the originals, including even faint marks or print.

- The subpoenaed entity or individual should put an identifying notation on each page of each document to indicate that it was produced by the subpoenaed entity or individual, and number the pages of all the documents submitted. (For example, if Jane Doe sends documents to the staff, she may number the pages JD-1, JD-2, JD-3, etc., in a blank corner of the documents). However, if the subpoenaed entity or individual sends the staff original documents, the subpoenaed entity or individual should not add any identifying notations.

- The subpoenaed entity or individual should make sure the notation and number do not conceal any writing or marking on the document.

- In producing a photocopy of an original document that contains post-it(s), notation flag(s), or other removable markings or attachments which may conceal all or a portion of the markings contained in the original document, photocopies of the original document both with and without the relevant post-it(s), notation flag(s), or removable markings or attachments should be produced.

Considerations:

In producing photocopies of the original copies, the subpoenaed entity or individual should be aware that:

- The SEC cannot reimburse the subpoenaed entity or individual for copying costs, except in the case of RFPA subpoenas.

- The subpoenaed entity or individual must maintain the originals of all copied documents responsive to the subpoena in a safe place in the event production of the original documents is required at a later date.

- If it appears that a photocopy of an original document may not represent the original document in its entirety, whether by means of post-it(s), notation flag(s), removable markings, erroneous copying, or any other reason, the staff should request the original document so that the staff can verify that the photocopy represents the original document in its entirety, including all of the markings contained within.

Further Information:

- Please refer any questions about the production of photocopied documents responsive to subpoenas to the Trial Unit.

- For more information concerning bates stamping of photocopied documents, please see Section 3.2.6.2.2 of the Manual.

### 3.2.6.2.2 Bates Stamping

Introduction:

Bates stamping (also known as Bates numbering or Bates coding) refers to the use of identifying numbers or date and time marks on images and documents as they are scanned or processed.

Bates stamping is commonly used as an organizational method to label and identify documents. Marking each document with a unique number is a useful tool both at the investigative stage and in litigation and provides an efficient and clear way to identify documents on the record in testimony and depositions.

Basics:

- Bates stamping assigns a unique identifier to each page produced or received during the course of an investigation or discovery. Such numbering may be solely numeric or may contain a combination of letters and number (alphanumeric).

- Although there is no standard method for numbering documents, the best practice is to place an identifying notation on each page of each document (1) to indicate the source of the production and (2) to number the pages of all the documents submitted.

- In cases of multiple productions by the same source, a production date (mm/dd/yy) may be stamped in addition to the letters used to identify the source of the production. For several productions from the same source, the best practice is to continue the numbering from the previous production.

- The notation and number should not conceal any writing or marking on the document.

- Manual Bates stamping involves the use of a self-inking stamp with six or seven numbered wheels that automatically increment each time the stamp is pressed down on a page. Preprinted, self-adhesive labels can also be used, as well as electronic document discovery (EDD) software that can electronically stamp documents stored as computer files by superimposing numbers of them. All produced documents should be imaged, and can be Bates stamped as they are imaged.

- If documents are produced already Bates stamped, there is no need to Bates stamp them a second time, unless the existing Bate stamp is duplicated in other documents. In that case, the best practice is to Bates stamp them with new sequence.

#### 3.2.6.2.3 Format for Electronic Production of Documents to the SEC

Introduction:

The staff is encouraged to request document production in electronic format. Documents, information, and data produced electronically may be delivered as: (1) scanned collections; (2) e-mail; or (3) native files. The formats for these types of productions should be communicated to parties wishing to produce documents, information, and data electronically. Staff should not accept electronic production of documents and information in any format other than these three formats (including databases) without prior discussions with, and approval from, the Division's IT staff.

Basics:

- Staff should request that each party producing documents and other information electronically organize each submission by custodian. Producing parties should also provide a summary of the number of records, images, emails, and attachments in the production so that the staff can confirm that the complete production has been loaded onto the SEC's computer system.

- The SEC currently uses Concordance 8.2 and Opticon 3.2 to review electronic document collections. All electronic productions should be compatible with these software systems.

- Data can be delivered on CD, DVD, or hard drive. The smallest number of media is preferred. If the collection is large enough to fit onto a hard drive, the SEC can provide one to the producing party, if needed.

- For scanned collections, each scanned file must contain four components: (a) image file; (b) delimited text file; (c) optical character recognition (OCR) text; (d) opticon cross-reference file. For further explanation and other information about the required four components, please contact the Division's IT staff.

- For electronic e-mail productions, there are several formats available, but it is preferable to request the producer of the e-mails to load them into a central repository or database and convert them into a searchable format that is compatible with Concordance. This method allows for the staff to run its own searches using its own search terms on the population of e-mails requested.

    - The preferred format for receiving electronically-produced email is delimited text with images and native attachments**.**

- The staff may also accept the following formats for electronic production of emails:

  - PST – a personal storage file native to Microsoft Office Outlook.

  - NSF – a personal storage file native to Lotus Notes.

- The staff should include the data standards described above in their document requests to ensure that the format of produced e-mails is loadable into Concordance and that the most relevant data fields are captured. If the producer of the e-mails wishes to negotiate alternative delivery standards, the staff should contact Division IT staff so that they can participate in the related discussions.

- Native files should be produced with an ASCII delimited file containing the media associated with the files, text extracted from the native file, and a directory path to the native file.

- A subpoena or document request should include the standard specific guidelines and instructions containing technical criteria to follow for producing documents electronically to the SEC.

Further Information:

For information on any aspect of electronic production, please consult the Division's IT staff.

#### 3.2.6.2.4 Privilege Logs

Basics:

With respect to each document that has been withheld from production on the grounds of any privilege or protection, the staff should request that a detailed privilege log be produced at the same time as the responsive documents. A failure to provide sufficient information to support a claim of privilege can result in a waiver of the privilege.

Considerations:

Please keep in mind the following considerations when requesting and reviewing privilege logs:

- Document requests or subpoena attachments should contain the following sample instruction:

  *If any requested document is withheld, please submit a list of all such documents that provides: (a) the identity and position of the creator(s); (b) the creation date; (c) the present or last known custodian; (d) a brief description, including the*

*subject matter; (e) the identity and position of all persons or entities known to have been furnished the document or a copy of the document, or informed of its substance; (f) the reason the document is not being produced and (g) the specific request in the subpoena to which the document relates.*

- After the initial production is received, the staff should ask for written confirmation that all requested materials have been produced and that any document withheld based upon an assertion of any privilege has been noted in the privilege log.

- The staff should carefully review the privilege log to determine whether the privilege has been properly asserted.

- The staff should obtain additional information where entries in the privilege log are incomplete or do not otherwise provide sufficient information to determine whether the privilege has been properly asserted.

- If a documentary privilege is asserted during testimony, the staff should stay on the record. The staff should exercise care when inquiring into potentially privileged matters by making clear on the record that they are not intending to obtain the disclosure of confidential communications between attorney and client. However, the staff should indicate on the record that they intend to establish whether the predicate facts for the assertion of the privilege are present.

#### 3.2.6.2.5 Business Record Certifications

Basics:

- At the time a company produces business records (e.g., telephone records, bank account statements, brokerage account records), the staff should simultaneously obtain from a custodian of records or other qualified person a declaration certifying that the documents are records of regularly conducted business activities.

- A certification should eliminate the need to have a custodian of records testify at deposition or civil trial because the records can be authenticated by the certification under Rules 902(11) and 902(12) of the Federal Rules of Evidence. A certification may also avoid the need for testimony by the custodian in an administrative proceeding.

Sample Certification:

[FOR DOMESTIC U.S. RECORDS]

**DECLARATION OF [*Insert Name*] CERTIFYING RECORDS OF REGULARLY CONDUCTED BUSINESS ACTIVITY**

I, the undersigned, [*insert name*], pursuant to 28 U.S.C. § 1746, declare that:

1. I am employed by [*insert name of company*] as [*insert position*] and by reason of my position am authorized and qualified to make this declaration. [*if possible supply additional information as to how person is qualified to make declaration, e.g., I am custodian of records, I am familiar with the company's recordkeeping practices or systems, etc.*]

2. I further certify that the documents [*attached hereto or submitted herewith*] and stamped [*insert bates range*] are true copies of records that were:

   (a) made at or near the time of the occurrence of the matters set forth therein, by, or from information transmitted by, a person with knowledge of those matters;

   (b) kept in the course of regularly conducted business activity; and

   (c) made by the regularly conducted business activity as a regular practice.

I declare under penalty of perjury that the foregoing is true and correct. Executed on [*date*].

_____

[*Name*]

[FOR FOREIGN RECORDS]

**DECLARATION OF [*Insert Name*] CERTIFYING RECORDS OF REGULARLY CONDUCTED BUSINESS ACTIVITY**

I, the undersigned, [*insert name*], declare that:

3. I am employed by [*insert name of company*] as [*insert position*] and by reason of my position am authorized and qualified to make this declaration. [*if possible supply additional information as to how person is qualified to make declaration, e.g., I am custodian of records, I am familiar with the company's recordkeeping practices or systems, etc.*]

4. I further certify that the documents [*attached hereto or submitted herewith*] and stamped [*insert bates range*] are true copies of records that were:

   (d) made at or near the time of the occurrence of the matters set forth therein, by, or from information transmitted by, a person with knowledge of those matters;

   (e) kept in the course of regularly conducted business activity; and

   (f) made by the regularly conducted business activity as a regular practice.

5. I understand that a false statement in this declaration could subject me to criminal penalty under the laws of [*country where declaration is signed*].

I declare under penalty of perjury under the laws of the United States of America that the foregoing is true and correct. Executed on [*date*] at [*place of execution*].

_____

[*Name*]

### 3.2.6.2.6. Confirming Completeness of Production

Introduction:

When recommending that the Commission accept a settlement offer from an entity or individual, it is important to obtain an executed Certification as to Completeness of Document Production from the settling party. In the Certification, the settling party acknowledges that the Commission has relied, among other things, upon the completeness of his production.

Basics:

- A settling individual must declare under penalty of perjury that he or she has made a diligent search of all files in his or her possession, custody, or control that are reasonably likely to contain responsive documents and that those documents have either been produced or identified in a privilege log.

- The Certification applies to SEC subpoenas, documents requests and requests for voluntary production of documents.

- In the case of an entity, the Certification should contain similar language, but require a representative to declare that he has made a diligent inquiry of all persons who reasonably had possession of responsive documents, and that those documents have been produced or identified in a privilege log.

### 3.2.6.3 Forthwith Subpoenas in Investigations

Basics:

A forthwith subpoena may be issued where there is a reasonable good faith basis for believing that there is a risk of destruction or alteration of the documents. A forthwith subpoena demands production "forthwith." For example, a forthwith subpoena may be issued if there is a danger that documents will be misplaced or destroyed unless produced immediately.

Though a forthwith subpoena may be appropriate in certain circumstances, staff should be aware that courts have raised concerns regarding its use. For example, some courts have not condoned the use of forthwith subpoenas (Consumer Credit Ins. Agency, Inc. v. U.S., 599 F.2d 770, 774 (6th Cir., 1979)), while other courts that have upheld forthwith subpoenas have cautioned against indiscriminate use (Wong Sun v. U.S., 371 U.S. 471, 83 S. Ct. 407 (1963)).

Considerations:

Staff should use forthwith subpoenas sparingly, when there is a reasonable good faith belief that a subpoena should require forthwith production. A reasonable good faith

basis for issuing a forthwith situation may include seeking documents from an individual or custodian (1) that is uncooperative or obstructive, (2) that is a flight risk, and (3) who may destroy, alter or otherwise falsify records.

Further Information:

If the staff is concerned that there is a risk of the destruction or alteration of documents that the staff intends to subpoena, the staff should consult with the Trial Unit immediately to ascertain whether issuing a forthwith subpoena would be appropriate under the circumstances.

#### 3.2.6.4 Maintaining Investigative Files

The Basic Requirement:

The Privacy Act requires that the SEC maintain records "with accuracy, completeness, timeliness, and relevance as is reasonably necessary to assure fairness to the individual in the determination." 5 U.S.C. Section 552a(e)(5).

Other Reasons for Maintaining Investigative Files:

- Following procedures to maintain investigative files helps ensure that any loss of or damage to the Division's offices, files, or equipment will cause minimal disruption to the work of the Division.
- Uniformity in document management practices helps facilitate information sharing and limit loss of information associated with staff turnover.
- Maintaining investigative files in a systematic way increases the likelihood of success in litigation. Investigative files need to be properly maintained so they can be shared with other law enforcement agencies. Rule 30-4(a)(7) of the SEC's Rules of Organization delegates to the Director of the Division of Enforcement authority to grant access requests to the SEC's non-public enforcement and regulatory files. An access grant generally provides authority to disclose both existing information and information acquired in the future to those entities listed in Rule 24c-1(b) of the Exchange Act.

The Basics of Maintaining Original Documents:

- Original documents received by the staff, whether informally or through subpoenas, should be segregated from personal notes, copies of internal e-mails, or any other documents.
- Original documents should be kept in pristine condition and no documents should be altered for any reason.
- In the event documents require additional protections (e.g., if they come from a foreign government and are not supposed to be transmitted pursuant to an access request), they should be kept separate and well marked.

The Basics of Maintaining Files:

- When a MUI is opened, the staff should implement a system for handling originals and hard copies of documents, including, but not limited to, correspondence, subpoenas, and third-party document productions. (For more information regarding Document Control, see Section 3.2.6.4.1 of the Manual.)
- When a MUI is opened, the staff should contact Enforcement IT staff to set up specific sub-directory on Enforcement's shared drive for the case. This subdirectory will follow Enforcement's standard "template," and will have four "top level" or main folders: (1) Commission Actions (capturing final versions of action memoranda, Commission Orders, Releases, etc.); (2) Investigation; (3) Litigation; and (4) Collections (which are in order of the progression of a typical Enforcement case). Each of these folders will have a number of sub-folders, including subpoenas, document production logs, data, contacts, etc. Staff should keep all electronic files required by and consistent with the investigation's "template."

Using Shared Drives:

Staff should maintain work product (e.g., subpoenas, internal memoranda, chronologies, pleadings), transcripts provided in electronic form, and documents produced to the staff in electronic form on shared drives.

Maintaining Internet Documents:

During the course of certain investigations, evidentiary issues may arise concerning authentication and preservation of Internet documents, particularly pertaining to pages from the World Wide Web. Web site publishers may, at any time and within seconds, edit, alter, or even remove the contents of their Web site. Upon discovering relevant evidence on a website, the staff immediately should take steps to preserve each individual relevant Web page. For information on how to preserve Web site evidence, see Section 3.2.6.4.2 of the Manual.

Preserving Electronically Stored Information ("ESI"):

Steps should be taken to preserve ESI in enforcement investigations. For further information on the preservation of ESI, see Section 3.2.6.4.1.2 of the Manual.

Special Considerations Pertaining to the Bank Secrecy Act ("BSA"):

All BAS information, such as Suspicious Activity Reports ("SARs"); Currency Transaction Reports ("CTRs") and Currency Transaction Reports by Casinos ("CTRCs"); Reports of Foreign Bank and Financial Interests ("FBARs"); Reports of International Transportation of Currency or Monetary Instruments ("CMIRs"); and Reports of Cash Payments Over $10,000 Received in Trade or Business, is highly confidential and must be segregated and labeled as sensitive. Steps must be taken to avoid inadvertent

dissemination of these documents or inadvertent disclosure of the existence of these documents. For further information, see Sections 2.2.2.1 and 4.7 of the Manual.

### 3.2.6.4.1 Document Control

Basics:

In implementing good document management and control during an investigation or litigation, the staff should have a structured and consistent system for labeling, storing, and keeping track of documents, which should indicate:

- what documents respondents, witnesses, or defendants have produced;
- when they produced the documents;
- in response to what subpoena or informal request; and
- whether the response to the subpoena or request is complete.

To that end, following are some general guidelines that the staff should strive to follow:

Labeling Documents:

- Subject to the considerations discussed below, all hard-copy productions should be bates stamped, either by the party producing them, or, if not, by the staff. For more information on bates stamping, see Section 3.2.6.2.2 of the Manual.

- If it is an electronic production, it is important to address labeling issues up front with producing party, before the documents are produced. For more information on the format for the electronic production of documents, see Section 3.2.6.2.3 of the Manual.

Keeping Track of Documents:

- The staff should index all documents after receipt, including those received in production, testimony transcripts, documents sent to off-site storage, etc. Each index should be saved on the appropriate sub-folder in the investigation's folder on Enforcement's shared drive.

- The staff should maintain logs/indexes of subpoenas issued, documents produced to the staff, testimony transcripts, etc., on the investigation's sub-directory located on the Division's shared drive.

Storage/Maintenance of Documents

Some "best practices," which would be helpful for staff to follow when storing and maintaining documents for a given matter, include clearly labeling documents,

segregating privileged documents from documents produced by third parties, and labeling/indexing documents to be stored off-site.

Use of Documents

Original documents should not be used for any reason except as necessary to present evidence in court or at a hearing. Therefore:

- Original documents should not be used as "working copies." They should not be marked or altered from their original production (except for bates stamping).

- The staff should make a copy if he/she needs to work with it, mark it up, or introduce it as an exhibit in testimony.

- Electronic data can be printed out or loaded onto the shared drive, which is a specially created queue to accept larger quantities of documents, with which the staff can work. The staff should keep an original, clearly labeled version of electronic production (CD or otherwise) that is not used for investigative purposes.

Further Information

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The staff should also consult with trial counsel regarding any concerns regarding the future use of documents in litigation.

#### 3.2.6.4.1.1 Document Imaging in Investigations

Introduction:

The Division, in coordination with the SEC's Office of Information Technology ("OIT"), has implemented a program to image evidentiary documents in investigations. The SEC's Electronic Documents ("EDOCS") program consists of two data management projects: the Electronic Production Project and the National Imaging Project.

The Electronic Production Project involves the loading of evidentiary materials from Division cases into an application called Concordance, which allows authorized staff to retrieve and view the documents. The National Imaging Project provides data back-up and disaster recovery for the program. It provides for the removal of voluminous evidentiary documents from Division premises in Headquarters and the regional offices. OIT, in consultation with the Division, manages the Electronic Documents program.

Basics:

- When evidentiary documents need to be imaged, the staff should submit a request to a Document Management Specialist ("DMA"), including the following

information: (1) case name; (2) location of documents; (3) case number; (4) priority; (5) source/producing party; and (6) any instructions or other specifics.

- The DMA will confirm the information, conduct any additional preparation of the documents, and either arrange to have the documents imaged onsite or outsource the imaging to a designated outside contractor.

- The DMA will send email notification to the appropriate staff, which will provide the necessary confirmation information.

- The documents will be scanned by the requested date, and will be hand delivered to the SEC for loading into the Concordance database shortly thereafter. The staff will receive notice when the imaging process has been completed.

- If the staff requests return of the documents, the imaging processing center will first retain the documents for 45 days after receipt, where they will be stored in a secured, limited access area so that random quality assurance checks can be done. However, if the staff requests that immediate return of the documents, they will be returned after the scanning has been completed.

- If the staff doesn't request the return of documents, the documents will be shipped to the Iron Mountain storage facility after the 45 day period, and confirmation and tracking information will be sent to the staff.

Further Information:

Please contact the Division's IT staff or OIT for further information on document imaging.

#### 3.2.6.4.1.2 Electronic Files

Introduction:

The procedures discussed below provide guidance and suggestions on how the Division staff should maintain files and records produced in electronic formats during the course of their investigations. The staff should strive to maintain and preserve all electronic files received from outside parties in an orderly manner during the course of their investigations and should not alter the original media and files.

Basics:

The staff may receive production of information in the form of CDs, DVDs, videotapes, audiotapes, and other electronic media, during the course of its investigations. Following are best practices to follow upon receipt of any type of electronic media:

- First, have a duplicate made by a qualified technician. The staff should consult with the Division's IT staff to determine which technician should duplicate a particular medium.

- Next, verify the type of information contained on the electronic medium in order to determine the best way to work with the files.

    - Text Files: If the information is in the form of text files, the staff will complete an "Electronic Data Submittal Form" and will submit the form, along with the duplicate medium, to the appropriate technician in OIT at the Home Office, who will load the contents of the duplicate medium onto the Home Office server. Both the original and duplicate will be returned to the staff. The information produced as the electronic file will be accessible to the staff via Concordance and on the duplicate medium.

    - Audio and Video Files: If the electronic medium contains audio or video files, the staff may have a transcript prepared of each duplicate recording. The transcript should identify the source of the recording (e.g., meeting, presentation, news video), each speaker, the speaker's location, and the dates and times the original recording was made. The transcript should also identify the name of the person who prepared it, the date the transcript was prepared, and any information sufficient to describe the specific medium (e.g., disc, tape) transcribed. The original and duplicate will be returned to the staff.

- Maintain all original files in a secure central location within each branch and the branch chief assigned to the investigation should be the designated custodian of the original files. Original files should not be used until necessary at trial or similar proceeding.

- Create and maintain a log for each original file. In the event an original file is to be removed from its secure central location, the staff member removing the file should sign the log and indicate the date and time the file was removed, as well as the date and time the file was returned to its secure location.

- The staff may access the electronic files on the duplicate copy itself and may also choose to load a copy of the duplicate recording onto the case file on the master drive of its office's computer system. The staff should use the duplicate files or transcripts, and not the original files or transcripts, during the investigation and discovery phase of litigation.

<u>Considerations</u>:

The staff should keep in mind that original files may ultimately be used at trial or during a similar litigation proceeding. Thus, the staff should take steps to avoid any

possible alteration to original electronic files, which will help preserve the integrity of all of its investigations.

Further Information:

- Please refer any questions about receiving, using, storing, and disposing of, electronic files to Enforcement's IT staff or OIT.

- For further information regarding audiotapes, please see Section 3.2.6.4.3.1 of the Manual.

- For further information on the format for electronic productions, please see Section 3.2.6.2.3 of the Manual.

#### 3.2.6.4.1.3 Complying with Federal Rule of Civil Procedure 26(a) Requirements and Preserving Evidence in Anticipation of Litigation

Basics:

Fed.R.Civ.P. 26(a)(1) requires the SEC to make certain disclosures at the onset of litigation. Additionally, the SEC is required to conduct a reasonable search of documents within its possession, custody, or control in order to respond to discovery requests pursuant to Fed.R.Civ. P. 34. Failure to produce documents during discovery can result in sanctions, including an order precluding the SEC from using those documents as evidence.

Simple Ways to Ensure Compliance:

Creating and maintaining an accurate *contact list* and *document index* will help the investigative staff effectively manage a complex investigation and greatly assist the SEC's trial attorneys when compiling initial disclosures pursuant to Rule 26(a)(1) and in responding to subsequent discovery requests.

*Contact list* – The contact list should include the name, address and telephone number of each individual likely to have discoverable information.

*Document index* - The document list should include all documents, electronically stored information, and tangible things ("documents") that the staff obtains during its investigation and provide at least the following:

- A description of the documents by category;

- Location of the documents;

- Identity of the party that produced the documents;

- Identification of the request/subpoena and correspondence relating to the documents; and

- Bates numbers, if possible.

Considerations:

Since the investigative staff may receive electronic production or scan a paper production into a Concordance database, once the documents are uploaded into Concordance it is particularly important to keep an accurate *document index* in order to satisfy the initial disclosure requirement in a timely manner.

Duty to Preserve Evidence

A duty to preserve electronically stored information ("ESI") and paper records generally arises when litigation is reasonably anticipated or foreseeable, as well as when litigation is pending. Failure to preserve ESI and paper records can result in Court sanctions. When there is a duty to preserve, Enforcement staff should make reasonable and good faith efforts to preserve ESI and paper records relevant to an investigation or litigation, including issuing a litigation hold notice to those individuals working for the SEC who are most likely to have relevant information directing them to preserve relevant ESI and paper records.

ESI is a broad term that includes word processing files, spreadsheets, databases, e-mail, and voicemail.

#### 3.2.6.4.1.4 Iron Mountain

Documents received by the staff in MUIs or investigations must be organized in boxes for transfer to Iron Mountain for storage:

- The boxes should include a detailed description of all contents to facilitate storage and retrieval.

- The staff should maintain tracking logs to include the date and location when boxes are sent to or received from Iron Mountain, and when boxes are destroyed or sent to Records Management.

- Each office should use a database to standardize the tracking process.

#### 3.2.6.4.2 Preserving Internet Evidence

Basics:

The most common form of Internet evidence is a website page. However, website owners may, at any time and within seconds, alter, edit or even remove contents of a website. Thus, upon discovering relevant evidence on a website, the staff immediately should seek to preserve that website evidence to capture information as it existed at the time the staff discovered the information.

Considerations:

The following procedures generally should be followed when preserving Internet evidence:

- The staff should ensure that, after saving a website page, each file contains the correct URL of the website and an electronic stamp of the date and time that each page was saved.

- The staff should also print these saved documents and affix an identifying mark on each page, such as a Bates stamp number. The printed page should include the URL of the website and the date and time of printing.

- The staff should maintain the original documents and several copies in a safe location.

- Be aware that these procedures only capture text and graphic (html) data on a website but do not include audio or video data.

Further information:

The staff should direct any questions about preserving Internet evidence to Enforcement's IT staff.

#### 3.2.6.4.3 Preserving Physical Evidence

The two most widespread forms of physical evidence in SEC investigations are audiotapes and electronic media hardware, such as computer hard drives. Usually, the staff will obtain copies of this data from the producing party in a commonly accessible format, such as cassette tapes for analog audio recordings, WAV files for electronic audio recording, and TIF or PDF files for electronic data stored on a hard drive.

However, there may be circumstances when the staff may need to obtain the original media source or obtain a copy that fully captures all data on the original media source, such as an image of an entire hard drive. The staff should consider obtaining

originals when there is a risk that the original media source may be destroyed or where the producing party cannot be relied upon to produce all relevant data on a media source. The original hardware also contains residual data, which can include deleted files.

Whether the staff obtains originals or copies, the staff generally should follow the procedures in Sections 3.2.6.4.3.1 and 3.2.6.4.3.2 of the Manual so that this physical evidence is preserved to ensure its authenticity.

### 3.2.6.4.3.1. Preserving Audiotapes

Audiotapes are usually produced in one of two ways. For digital recordings, audio recordings are produced as WAV files on CD-roms or DVDs. For analog recordings, the recordings are often produced on audio cassette tapes. In either format, the staff should be able to trace the receipt and custody of audiotape data from the time they are received through their use at trial and demonstrate that the audiotapes were securely stored once they came into the staff's possession. The goal is to ensure the admissibility of the recording by establishing its authenticity and the requisite preservation of its condition.

To maintain authenticity, the staff should follow these procedures:

- When obtained, audiotapes should be affixed with a Bates or control number.

- Testimony of the tape's custodian should establish the producing party's procedures for making and maintaining audiotapes, the procedures used to produce the audiotapes to the SEC and the location of the originals (if copies were produced). The custodian should also be asked to identify the date and time of the recordings, and the speakers and the source of the recording, such as the telephone numbers associated with the recording. This information is often available in digital recordings by retrieving data files created at the time the recording was made that capture this information.

- If copies are produced, the staff should ensure the custodian testifies on the record that he understands the obligation to maintain the originals in a place and manner sufficient to preserve their authenticity.

- If original recordings are produced, the staff should keep the originals in a safe location and use copies during the course of the investigation. A log should be created and maintained that requires any individual that retrieves the originals to document the date and time that the originals were checked out and in.

- The staff should have transcripts prepared of all audiotapes with evidentiary value.

### 3.2.6.4.3.2 Preserving Electronic Media

Basics:

Electronic media hardware that may be useful during an investigation includes computer hard disk drives, CDs or DVDs, backup tapes, USB flash drives, personal data assistants ("PDAs"), and cellular phones. The staff should establish the authenticity of the hardware and prevent against any alteration or destruction of information as follows:

- When obtained, electronic media hardware should be affixed with a Bates number.

- The staff should store original hardware in a safe location, use only copies of the data during the investigation, and create a log to document all circumstances when the originals are removed from their storage location.

- Through the testimony of the owner of the hardware or the custodian charged with maintaining hardware, the staff should seek to establish the authenticity of the original hardware, including information regarding the procedures utilized for storing data and maintaining data on the hardware

Considerations:

The staff may also obtain an image of all data located on the hardware instead of the original. Imaging is a copying process that produces an exact digital replica of the original data on the hardware and preserves the structure and integrity of the data. The staff should confer with Enforcement's IT staff to ensure proper imaging of data. To be deemed reliable, the imaging of electronic media information must meet industry standards for quality and reliability, must ensure that no data is altered during the imaging process, and must be tamper proof. The Enforcement IT staff has established specific procedures and guidelines for imaging data. The staff should also ensure that the producing party has stored the originals in a safe location, including confirming details of such storage through the testimony of a custodian or owner of the hardware.

Further Information:

- Please refer any questions about preserving electronic media evidence to the Division's IT staff.
- *See* Section 3.2.6.4.1.1 of the Manual for more information on imaging.
- *See* Section 3.2.6.4.1.2 of the Manual for more information on electronic files.

## 3.3 Witness Interviews and Testimony

### 3.3.1 Privileges and Privacy Acts

In connection with any witness interviews or testimony, staff must comply with the Privacy Act of 1974, the Right to Financial Privacy Act of 1978, and the Electronic Communications Privacy Act of 1986 and the rules regarding the assertion of privileges, contacting witness's counsel, parallel proceedings, ongoing litigation, and Freedom of Information Act requests. Those rules and statutes are discussed in Section 4 of the Manual.

### 3.3.2 No "Targets" of Investigations

Unlike the grand jury process in which targets of an investigation are often identified, the SEC investigative process does not have "targets." Thus, the SEC is not required to provide any type of target notification when it issues subpoenas to third parties or witnesses for testimony or documents in its non-public investigations of possible violations of the federal securities laws. The Supreme Court, in *SEC v. O'Brien*, 467 U.S. 735 (1984), noted that "the imposition of a notice requirement on the SEC would substantially increase the ability of persons who have something to hide to impede legitimate investigations by the Commission." Citing the SEC's broad investigatory responsibility under the federal securities laws, the Court found no statutory, due process, or other standard regarding judicial enforcement of such subpoenas to support the proposition that notice is required.

Although some parties involved in investigations eventually may be named as defendants or respondents in subsequent litigation, the SEC does not have targets of its inquiries or investigations.

### 3.3.3 Voluntary Telephone Interviews

#### 3.3.3.1 Privacy Act Warnings and Forms 1661 and 1662

Basics:

- The Privacy Act of 1974 ("Privacy Act"), 5 U.S.C. Section 552a, requires, among other things, certain disclosures to individuals from whom the SEC's staff solicits information.

- When the staff contacts a person to request a voluntary telephone interview, before asking any substantive questions, the staff should provide an oral summary of certain information contained in Form 1661 or 1662, as appropriate (*see* Section 3.2.3.1 of the Manual), including at least the required Privacy Act information.

- The Privacy Act requires that the staff provide the following information:
    - That the principal purpose in requesting information from the witness is to determine whether there have been violations of the statutes and rules that the SEC enforces.
    - That the information provided by members of the public is routinely used by the SEC and other authorities, to conduct investigative, enforcement, licensing, and disciplinary proceedings, and to fulfill other statutory responsibilities.
    - That the federal securities laws authorize the SEC to conduct investigations and to request information from the witness, but that the witness is not required to respond.
    - That there are no direct sanctions and no direct effects upon the witness for refusing to provide information to the staff.

Considerations:

When appropriate, the staff also sends a Form 1661 or 1662 (along with a cover letter) to the witness after the telephone interview has taken place. If practicable, for example, if the staff contacts the witness and the witness asks to delay the interview to a later date, the staff may send the Form 1662 in advance of the telephone interview.

#### 3.3.3.2 Notetaking

Basics:

While conducting a voluntary telephone interview, the staff may take written notes of the interview.

Considerations:

A minimum of two staff members are encouraged to be present to conduct a witness interview. However, for litigation reasons, staff should consider having only one staff member take notes.

Advantages to having a minimum of two staff members present to conduct a witness interview include having more than one person who can ask questions and later have recollections and impressions of the interview. Moreover, one of the staff members may subsequently need to serve as a witness at trial.

### 3.3.4 Voluntary On-the-Record Testimony

Basics:

The staff may request voluntary transcribed ("on the record") testimony from witnesses. The staff cannot require and administer oaths or affirmations without a formal

order of investigation. Nevertheless, the staff can conduct voluntary interviews with a court reporter present and a verbatim transcript is produced.

If a witness is voluntarily willing to testify under oath, the staff, after obtaining the witness's consent, will have the court reporter place the witness under oath. If the witness is placed under oath, false testimony may be subject to punishment under federal perjury laws. In addition, 18 U.S.C. Section 1001, which prohibits false statements to government officials, applies even if a witness is not under oath.

While conducting voluntary on-the-record testimony, the witness may have counsel present. Also, at the beginning of the testimony, the staff should consider asking the witness questions on the record to reflect that the witness understands: (1) that the witness is present and is testifying voluntarily; (2) that the witness may decline to answer any question that is asked, and (3) that the witness may leave at any time.

Considerations:

Staff can otherwise conduct the voluntary on-the-record testimony as it would any other testimony, including providing the witness with the Form 1662 prior to testimony.

### 3.3.5 Testimony Under Subpoena

#### 3.3.5.1 Authority

The SEC may require a person to provide documents and testimony under oath upon the issuance of a subpoena. Prior to issuing any subpoenas in a matter, the staff must obtain authorization from the Commission through the issuance of a formal order of investigation. Pursuant to 17 C.F.R. Section 202.5(a), the Commission, may, in its discretion, issue a formal order of investigation to determine whether any person has violated, is violating, or is about to violate any provision of the federal securities laws or the rules of a self-regulatory organization of which the person is a member or participant.

In authorizing the issuance of a formal order of investigation, the Commission delegates broad fact-finding and investigative authority to the staff. Various statutes provide for the designation of officers of the Commission who can administer oaths, subpoena witness, take testimony, and compel production of documents. *See* Sections 8(e) and 20(a) of the Securities Act, Sections 21(a)(1) & (2) of the Exchange Act, Section 209(a) of the Advisers Act, and Section 42(a) of the Investment Company Act. These statutory provisions do not limit the designation of Commission "officers" to attorneys. Staff accountants, analysts, and investigators also may be designated as "officers" and empowered to take testimony and issue subpoenas.

Rule 7(a) of the SEC's Rules Relating to Investigations, 17 C.F.R. Section 203.7(a), provides that any person who is compelled or required to furnish documents or testimony in a formal investigation shall, upon request, be shown the formal order of

investigation. A witness also may submit a written request to the Assistant Director of the Division of Enforcement supervising the investigation for a copy of the formal order.

### 3.3.5.2 Basic Procedures for Testimony Under Subpoena

#### 3.3.5.2.1 Using a Background Questionnaire

Basics:

The background questionnaire is a document that the SEC staff uses to obtain important background information from a witness. The questionnaire solicits a variety of personal information from the witness, including, among other things, the date and place of birth, the names and account numbers for all securities and brokerage accounts, a list of all educational institutions attended and degrees received, and an employment history. The information solicited in the background questionnaire is routinely asked for in testimony.

Considerations:

- The witness does not have to comply with the SEC staff's request to complete the background questionnaire. Disclosure of the information is entirely voluntary on the witness's part. There are no direct sanctions and thus no direct effects for failing to provide all or any part of the requested information, although it should be explained that this information will then be asked for in testimony.
- If the witness chooses to provide a background questionnaire, the witness should be examined about the document. For example, the witness should be asked to authenticate the document, by requiring the witness to testify about its preparation, the source of information contained in the document and the accuracy of the information.
- Information provided pursuant to a background questionnaire is subject to the SEC's routine uses as listed in Form 1662. The witness also is liable, under Section 1001 of Title 18 of the United States Code, if he or she knowingly makes any false statements in the background questionnaire.
- Background questionnaires, as exhibits to testimony transcripts, may become public if they are produced during discovery in a subsequent litigation. Therefore, in order to safeguard sensitive personal information, the staff may consider not including a witness's Social Security number in the Background Questionnaire. Likewise, the staff may consider not having a witness's Social Security number be recorded (and therefore included in the testimony transcript). Rather, the staff taking the testimony can ask the witness to write his/her Social Security number on a separate document. After presenting the document to the staff, the witness should verify that the information contained in it is correct.

#### 3.3.5.2.2. Witness Right to Counsel

Basics:

- Any person compelled to appear, or who appears by request or permission of the SEC, in person at a formal investigative proceeding may be accompanied, represented and advised by counsel, provided, however, that all witnesses shall be sequestered, and unless permitted in the discretion of the officer conducting the investigation no witness or the counsel accompanying any such witness shall be permitted to be present during the examination of any other witness. *See* Rule 7(b) of the SEC's Rules Relating to Investigations, 17 C.F.R. Section 203.7(b).

- This means that a testifying witness may have an attorney present with him or her during any formal investigative proceeding, and the attorney may (1) advise the witness before, during and after the testimony; (2) question the witness briefly at the conclusion of the testimony to clarify any of the answers the witness gave during testimony; and (3) make summary notes during the witness's testimony solely for the witness's use. *See* Rule 7(c) of the SEC's Rules Relating to Investigations, 17 C.F.R. Section 203.7(c). If the witness is accompanied by counsel, he or she may consult privately.

- "Counsel" is defined as any attorney representing a party or any other person representing a party pursuant to Rule 102(b) of the SEC's Rules of Practice, 17 C.F.R. Section 201.102(b). *See* Rule 101(a) of the SEC's Rules of Practice, 17 C.F.R. Section 201.101(a).

- Rule 102(b) of the SEC's Rules of Practice states that in any proceeding a person may be represented by an attorney at law admitted to practice before the Supreme Court of the United States or the highest court of any State (as defined in Section 3(a)(16) of the Exchange Act, 15 U.S.C. Section 78c(a)(16)); a member of a partnership may represent the partnership; a bona fide officer of a corporation, trust or association may represent the corporation, trust, or association; and an officer or employee of a state commission or of a department or political subdivision of a state may represent the state commission or the department or political subdivision of the state.

Considerations:

- If a witness is not accompanied by counsel, the witness may advise the SEC employee taking the testimony at any point during the testimony that he or she desires to be accompanied, represented and advised by counsel. The testimony will be adjourned to afford the witness an opportunity to arrange for counsel.

- The witness may be represented by counsel who also represents other persons involved in the SEC's investigation. For more information on Multiple Representations, see Section 4.1.1.1. of the Manual.

#### 3.3.5.2.3 Going off the Record

Basics:

The SEC employee taking the testimony controls the record. If a witness desires to go off the record, the witness must indicate this to the SEC employee taking the testimony, who will then determine whether to grant the witness's request. The reporter will not go off the record at the witness's, or the witness counsel's, direction. *See* Form SEC 1662 *and* Rule 6 of the SEC's Rules Relating to Investigations, 17 C.F.R. Section 203.6.

#### 3.3.5.2.4 Transcript Availability

Basics:

Transcripts, if any, of formal investigative proceedings shall be recorded solely by the official reporter, or by any other person or means designated by the officer conducting the investigation. A person who has submitted documentary evidence or testimony in a formal investigative proceeding shall be entitled, upon written request, to procure a copy of his documentary evidence or a transcript of his testimony on payment of the appropriate fees: *Provided, however,* that in a nonpublic formal investigative proceeding the Commission may for good cause deny such request. In any event, any witness, upon proper identification, shall have the right to inspect the official transcript of the witness's own testimony. *See* Rule 6 of the SEC's Rules Relating to Investigations, 17 C.F.R. Section 203.6.

If the witness wishes to purchase a copy of the transcript of his or her testimony, the reporter will provide the witness with a copy of the appropriate form. Persons requested to supply information voluntarily will be allowed the rights provided by this rule.

Further Information:

Assigned staff should consult with his/her supervisor for the procedures to be followed in order to make a recommendation that the SEC deny a witness's request for a transcript copy.

### 3.3.5.3 Special Cases

#### 3.3.5.3.1 Witness Assurance Letters

Introduction:

In some very limited circumstances, the staff may provide a witness with a letter assuring him or her that the SEC does not intend to bring an enforcement action against

him or her or an associated entity. In return, the witness agrees to provide testimony and documents and information. The provision of a written assurance letter must be specifically authorized by the Commission, and the circumstances under which to recommend the Commission provide such an assurance letter are narrow.

Considerations:

Some of the considerations in determining whether to recommend that the Commission provide a written assurance to a witness include:

- Is the Commission unable to seek testimony from the witness in any other fashion? For example, the Commission cannot compel the testimony due to a lack of jurisdiction, the United States and foreign domicile do not have a Memorandum of Understanding that allows the Commission to seek or compel testimony, and the witness refuses to testify or provide information voluntarily.

- Will the witness provide evidence crucial to an enforcement action against others? Is it impracticable to obtain the evidence from other sources?

- Based on current knowledge, should the witness be the subject of a recommendation for an enforcement action?

Procedures:

If the staff has determined that a witness assurance letter is both necessary and appropriate, the staff must prepare an action memorandum to the Commission. The memo should include name of a specific designee to sign the written assurance (for example, recommend "that the Commission authorize [Assistant Director], or his/her designee, to provide a key witness with a written assurance (attached), that the Commission does not currently intend to bring an enforcement action against him/her.").

In addition, because the written assurance refers to "information currently known to the Commission," the staff should prepare a dated inventory of all files (including interview notes), documents, and transcripts obtained or prepared prior to providing the written assurance.

Sample Witness Assurance Letter:

Re: In the Matter of [Issuer, Inc.], [Matter Number]

Dear Mr. [Witness]:

The Securities and Exchange Commission (the "Commission"), [Company], and [Company's] [Chief Financial Officer/position], [Witness], in both his personal and corporate capacities at [Company], agree as follows:

1. [Witness] agrees to make himself available to testify in any action against any persons and/or entities arising from the Commission's investigation in the matter of [Issuer, Inc.], including, but not limited to, any Commission action against [Issuer] and/or its current or former officers, directors, employees, auditors, underwriters, counsel or customers ("[Issuer] SEC Litigation"), if necessary, upon reasonable notice at a place to be agreed upon.

2. Based upon the information currently known to the Commission, it does not intend to file an action against [Witness] or [Company] arising from its investigation in the matter of [Issuer, Inc.]. This letter should not be deemed an exoneration, or be used to construe that the Commission has made a finding that no violations of the federal securities laws have occurred.

3. [Witness'] agreement to appear at a deposition in the [Issuer] SEC Litigation does not constitute an agreement by [Witness] or [Company] as to the extraterritorial application of U.S. securities law or the jurisdiction of the Commission in any action involving [Witness] or [Company].

4. [Witness] agrees to cooperate completely and truthfully with the Commission. He will answer completely and truthfully all questions put to him and disclose all relevant conduct about which he has knowledge. He will not withhold any information or attempt to protect any person by providing false information or by failing to reveal information. He will not falsely implicate any person. He and [Company] will voluntarily furnish to the Commission documents or other records in their possession involving specified transactions with [Issuer] and other companies during [relevant time period].

5. In return for [Witness'] and [Company's] full and truthful cooperation, as set forth herein, the Commission agrees not to use any statements or other information made by [Witness] or [Company] to the Commission or in testimony before any court or other tribunal in the [Issuer] SEC Litigation (or any information derived directly or indirectly therefrom) against either of them in any proceeding brought by the Commission after the date of this agreement, except that the Commission may share the information with appropriate authorities in a prosecution for perjury, making a false statement or obstruction of justice.

6. If [Witness] or [Company] knowingly provides false or misleading testimony or information, or fails to disclose all relevant conduct of which he is aware, or otherwise violates any term of this agreement, then this agreement shall be null and void. Thereafter, any testimony or other information provided by [Witness] or [Company] may be used against them without limitation for any purpose in any proceeding.

If [Witness] and [Witness' counsel] agree that this letter accurately reflects the entire agreement between [Witness] and the Commission, please sign in the appropriate places below and return the executed copy to me.

Very truly yours,

_____

[Designee],
[Title],
[Office]
U. S. Securities & Exchange Commission

Acknowledged and agreed to:

_____ _____

[Witness], Date
Individually and on behalf of [Company]

_____ _____

[Witness' Counsel], Esq. Date

### 3.3.5.3.2 Immunity Orders

Authority:

Title 18 of the Organized Crime Control Act of 1970, 18 U.S.C. Sections 6001-6004, provides that, where certain criteria are met and upon approval by the Attorney General of the United States[5], the Securities and Exchange Commission may issue an order

[5] 28 C.F.R. Section 0.175 provides that certain officials within the Department of Justice may exercise the authority vested in the Attorney General under 18 U.S.C. Section 6004 to approve agency immunity orders, including Assistant and Deputy Attorney Generals.

granting immunity from criminal prosecution to a witness in an investigation and compelling his or her testimony and other information.[6]

Basics:

The issue of granting immunity to a witness in SEC investigations arises where the witness asserts his or her Fifth Amendment privilege against self-incrimination and, accordingly, refuses to answer questions and provide other information.

Immunity orders are granted in limited circumstances and staff should consult their supervisors before recommending that the Commission issue an immunity order. If the staff believes that seeking an immunity order is an appropriate step, the staff should seek Commission authority to do so in an action memorandum. The statutory requirements for issuing an immunity order provide that the Commission must, in its judgment, determine that: (1) the testimony or other information from the witness may be necessary to the public interest; and (2) the witness has refused, or is likely to refuse, to testify or provide other information on the basis of his or her privilege against self-incrimination. 18 U.S.C. Section 6004.

The type of immunity permitted under the statute is "use immunity," which prohibits the government from using a witness's compelled testimony, or any information directly or indirectly obtained from that testimony, against the witness in connection with criminal prosecution of the witness, except in a prosecution for perjury, false statement, or failure to comply with the order. Use immunity conferred to a witness in SEC investigations will not, however, shield that witness from liability in civil proceedings. The SEC can still bring civil or administrative proceedings against the witness based upon the immunized testimony. If the Commission issues an order immunizing the witness and compelling testimony, the witness can no longer continue to refuse to testify either in the investigation or in a related enforcement action.

Considerations:

The staff does not have authority to grant immunity to any witnesses, without approval of the Attorney General and a Commission order. In this regard, it is advisable to consult with the appropriate U.S. Attorney's office prior to starting the formal process for obtaining witness immunity. Further, the staff should be cognizant of "inadvertent immunity" grants, which may occur if a witness testifies after claiming the Fifth Amendment privilege against self-incrimination. The staff can seek to prevent claims that questions posed after a witness's assertion of the Fifth Amendment privilege confer immunity by stating on the record that it has no authority to confer immunity, that it has no intention of doing so, and that any questions asked from that point on in the testimony

[6] *See U.S. v. Doe*, 465 U.S. 605 (1984) ( the Court held that, although the content of business records is not privileged, the act of producing records of a sole proprietorship may be self-incriminating and cannot be compelled without a statutory grant of use immunity).

will be with the understanding that the witness may decline to answer on the basis that the response may tend to incriminate the witness. Without compulsion to testify, there can be no claim that immunity was granted. *U.S. v. Orsinger*, 428 F.2d 1105, 1114 (D.C. Cir.), *cert. denied*, 400 U.S. 831 (1970) (witness who refused to testify under Commission subpoena, and who was not compelled to testify, acquired no immunity from criminal prosecution). *See also U.S. v. Abrams*, 357 F.2d 539, 549 (2d Cir.), *cert. denied*, 384 U.S. 1001 (1966).

#### 3.3.5.3.3 Contacting Employees of Issuers

ABA Model Rule of Professional Conduct:

In conducting investigations, the staff should adhere to the standard set forth in American Bar Association Model Rule of Professional Conduct 4.2 ("Model Rule 4.2") and commentary and ethics opinions interpreting that Rule, which addresses attorney communications with persons, including corporations and their employees, represented by counsel. Model Rule 4.2 provides:

> In representing a client, a lawyer shall not communicate about the subject of the representation with a person the lawyer knows to be represented by another lawyer in the matter, unless the lawyer has the consent of the other lawyer or is authorized to do so by law or a court order.

The staff should be mindful of this policy, and take it into account when determining whether to go through corporate counsel to contact corporations and their employees during the investigative process.

Basic Guidelines for Contacting Employees of Issuers:

- In the absence of a compelling reason to contact an individual directly, staff should go through corporate counsel (if such counsel exists) to contact corporate employees in the following categories:
    - employees who have a managerial responsibility on behalf of the organization, e.g., senior officers;
    - employees who supervise, direct, or regularly consult with the corporate counsel concerning the matter that is the subject of the investigation or if the persons have power to compromise or settle the matter;
    - employees whose acts or omissions may be imputed to the organization for purposes of civil or criminal liability in the matter; or

- employees whose statements, under applicable rules of evidence, would constitute an admission on the part of the organization or have the effect of binding the organization with respect to proof of the matter.

- If corporate counsel has made no assertion that he or she represents any particular group of employees that do not fall within the above categories, staff may contact such an employee directly, unless staff is aware of an attorney who represents that person in its investigation.

- When contacting employees directly, staff should inquire whether the employee is represented by counsel, including corporate counsel. According to the ABA Committee on Ethics and Professional Responsibility, Model Rule 4.2 has some limits: Formal Opinion 95-396 notes that the Model Rule "does not contemplate that a lawyer representing the [corporate] entity can invoke the rule's prohibition to cover all employees of the entity, by asserting a blanket representation of all of them."

- Contacting former employees without first contacting corporate counsel is generally permissible, unless corporate counsel (or, of course, the employee) has affirmatively stated that corporate counsel has been retained by that particular former employee. Restatement of Law Governing Lawyers, Comment G, provides that, "contact with a former employee or agent ordinarily is permitted, even if the person had formerly been within a category of those with whom contact is prohibited." However, Section102 of the Restatement provides that, "a lawyer communicating with a nonclient…may not seek to obtain information that the lawyer reasonably should know the nonclient may not reveal without violating a duty of confidentiality to another imposed by law." Accordingly, staff should be sensitive to potentially privileged corporate communications when seeking information from the former employee.

#### 3.3.5.3.4. Communications With Employees of Broker-Dealers

Basics:

While the Exchange Act requires brokerage firms to produce certain information upon request from the SEC and without an investigative subpoena, the Exchange Act does not require employees of brokerage firms to cooperate with inquiries into the employee's individual conduct. Therefore, an employee of a brokerage firm may or may not cooperate voluntarily with the Division's inquiries into the employee's individual conduct.

When the scope of an investigation touches upon an employee's duties at his or her current brokerage firm, the staff typically should communicate with the employee through the firm's general counsel or compliance officer.

Exceptions:

- The Division staff typically does not contact the brokerage firm's general counsel or compliance officer to speak to an employee when inquiring about matters outside the scope of the employee's duties at his or her current firm. For example, the staff typically contacts the employee directly when seeking information related to an employee's prior employment or when the staff is inquiring about matters outside of the scope of the employee's duties. These practices stem from, among other considerations, respect for an employee's privacy with regard to his or her employer.

- The staff also typically contacts the employee directly when the employee is a whistleblower. Considerations in the whistleblower context include the threat of retaliation. Assigned staff should consult with their supervisors to discuss the concerns that may arise in the whistleblower context.

### 3.3.5.3.5 Contacting Witness Residing Overseas

Basics:

The staff is encouraged to consult with the Office of International Affairs ("OIA") as soon as the staff suspects any foreign connection to an investigation. Because countries have varying requirements for contacting witnesses, Division staff should contact OIA before attempting to contact a witness residing overseas. OIA can provide advice on the existence of any information sharing mechanism in the country in which the witness resides, the uses to which information can be put, and practical considerations, such as likely response time for the assistance needed from a particular country. OIA also can prepare requests to foreign authorities and review drafts by Division staff for compliance with the requirements of any information sharing mechanism that exists and or foreign law and practice. Depending on the needs of a particular case, OIA may arrange conference calls or other meetings with the foreign counterpart, sometimes in advance of sending a formal request for assistance.

Considerations:

As a general matter, the Division is able to obtain testimony from witnesses residing overseas through a variety of mechanisms. These mechanisms include: information sharing arrangements with foreign counterparts such as memoranda of understanding; mutual legal assistance treaties; letters rogatory; ad hoc arrangements; and voluntary cooperation OIA can advise the Division staff as to which of these mechanisms is available in a particular foreign jurisdiction.

- Memoranda of Understanding ("MOUs")

  MOUs are regulator-to-regulator arrangements regarding information sharing and cooperation in securities matters. The SEC has entered into over 30 such sharing arrangements with its foreign counterparts. The SEC is also a signatory to the

International Organization of Securities Commissions Multilateral MOU. This MOU is the first global information sharing arrangement among securities regulators.

The scope of information that the SEC can obtain pursuant to an MOU varies depending on the legal abilities of the particular foreign authority. Some, but not all, MOUs allow for the SEC to obtain witness statements.

- Mutual Legal Assistance Treaties ("MLATs") (Criminal Matters)

  Generally, MLATs are designed for the exchange of information in criminal matters and are administered by the Department of Justice ("DOJ"). Despite the fact that MLATs are primarily arrangements to facilitate cross-border criminal investigations and prosecutions, the SEC may be able to use this mechanism in certain cases. Some jurisdictions permit the SEC to obtain information, including sworn testimony, through MLATs. U.S. criminal interest in the matter may be a prerequisite to the ability of the SEC to obtain information through MLATs. DOJ has signed numerous MLATs through foreign criminal authorities. MLATs may be an effective mechanism to obtain assistance when an MOU with a particular country either does not exist or does not permit the type of information sought from a witness residing overseas.

- Letters Rogatory

  A Letter Rogatory is a formal request from a court in one country to the appropriate judicial authority in another county. Generally, a Letter Rogatory is used in litigation to request compulsion of testimony or other evidence, or to serve process on a person located abroad. The execution of a request for judicial assistance by the foreign court is based on comity between nations, absent a specific treaty such as the Hague Convention on the Taking of Evidence Abroad in Civil or Commercial Matters. Because a Letter Rogatory generally can only be used to gather evidence in litigation, a Letter Rogatory may have limited utility where a case is in the investigative stage.

- Ad Hoc Arrangements

  Even if no formal information sharing mechanism exists with respect to a particular jurisdiction, the SEC nevertheless may be able to secure assistance in contacting a witness overseas by working on an *ad hoc* basis with foreign authorities. Such *ad hoc* arrangements often prove particularly helpful with emerging markets, whose securities legislation continues to develop.

- Voluntary Cooperation

  Depending on the jurisdiction, it may be possible to request information directly from persons located abroad on a voluntary basis. However, in some countries

such efforts may violate local statutes and laws. In still other jurisdictions, advance notice to the local regulator and relevant authorities may be required. Division staff should consult OIA even where the staff seeks only voluntary cooperation from a witness. Where seeking voluntary cooperation, the staff should stress the voluntary nature of the inquiry.

Further Reference:

For more information on contacting witnesses residing overseas, please contact OIA.

#### 3.3.5.4 Proffers Agreements

Basics:

In certain limited circumstances, the staff, with the approval of an Assistant Director or higher, may enter into a proffer agreement with a witness. A proffer letter (also known as a "Queen for a Day" letter) is a written agreement between the staff and the witness stating that, among other things, the oral statements made by the witness during a specified meeting date will not be used against the witness in any enforcement proceeding that may subsequently follow. Proffer agreements should not be granted without serious consideration and consultation with supervisors since doing so may potentially impact the staff's ability to bring a case against the witness. Nonetheless, such an agreement can be particularly helpful if the witness can provide the staff with evidence that the staff may not otherwise be able to obtain and/or assist the staff in developing leads to new evidence.

Considerations:

Protections:

Certain protections are afforded by the proffer agreement which should be made clear to the witness. As already stated above, any statements made by the witness at the meeting cannot be used against the witness pursuant to the agreement. However, if the staff discovers that the witness has given false statements during the meeting, then those statements may be used against the witness for possible obstruction of justice charges. Also, a witness's statements may be used to impeach the witness during cross-examination or to rebut any contrary evidence offered by the witness in any subsequent civil or administrative proceeding. The protections provided in the proffer agreement do not apply to statements made by the witness at any other time outside of the specified meeting date stated in the proffer letter.

Joint Proffer Sessions:

If the staff conducts a joint proffer session with the criminal authorities, the staff is encouraged to address any potential substantive or procedural issues with his or her supervisors, as well as the Assistant United States Attorney on the case, before the proffer begins. In cases where the staff participates in a proffer with the criminal authorities and the witness has not asked for a proffer letter from the SEC, the staff should remind the witness that the proffer agreement with the criminal authorities does not apply to the SEC.

Standard Proffer Agreement:

The staff typically uses a standard proffer agreement (below), and the staff should not agree to modifications to the standard agreement without first consulting with the Office of Chief Counsel and/or the Head of the Trial Unit. The proffer agreement must be signed by a supervisor at or above the level of Assistant Director.

[SEC LETTERHERAD]

[*Date*]

[*name of witness*
*c/o name of attorney*
*address of attorney*]

Re: In the Matter of [*name*], File No. HO-[*number*]

Dear [*name of witness*]:

This is to confirm the terms of the [*insert date*] meeting (the "Meeting") between you and the staff of the Division of Enforcement of the United States Securities and Exchange Commission in connection with the above-referenced matter. The meeting is subject to the following guidelines and conditions:

(1) With respect to any civil or administrative actions brought against you by the Commission or its staff, the Commission will not offer at any trial or other proceeding, any statements made by you at the Meeting, except with respect to false statements made at this Meeting evidencing obstruction of justice, perjury, or other violations of law based upon the inaccuracy or incompleteness of the statements;

(2) Notwithstanding paragraph (1) above, the Commission and its staff may use: (a) information derived directly or indirectly from the Meeting for the purpose of obtaining leads to other evidence, which evidence may be used in any civil action or administrative proceeding against you by the Commission; and (b) statements made by you at the Meeting and all evidence obtained directly or indirectly therefrom for the

purpose of cross-examination should you testify, or to rebut any evidence offered by you or on your behalf in connection with any civil action or with any administrative proceeding, should any be undertaken;

(3) It is further understood that this Agreement is limited to the statements made by you at the Meeting and does not apply to any oral, written or recorded statements made by you at any other time;

(4) No understandings, promises, agreements and/or conditions have been entered into with respect to the Meeting other than those set forth above in paragraphs (1) through (3) of this letter and none will be entered into unless in writing and signed by the parties to this agreement; and

**IF APPLICABLE, ADD:**

**(5) This letter does not limit or otherwise affect any understandings set forth in any agreement between you and the [*add appropriate prosecutor's office*], and any agreement between you and the [*add appropriate prosecutor's office*] does not limit or otherwise affect the understandings and conditions set forth in this letter.**

Sincerely,

[*name*]
Assistant Director

The foregoing is understood and agreed to by:

_____ _____
[*Name of Witness*] Date

Approved as to form:

_____
[*name of attorney for witness*]
Counsel to [*name of witness*]

## 4. Privileges and Protections

### 4.1 Assertion of Privileges

#### 4.1.1 Attorney-Client Privilege

Basics:

- The attorney-client privilege protects from disclosure confidential communications between attorney and client made when the client is seeking legal advice. The purpose of the privilege is to encourage free and candid communication between attorney and client.

- Elements necessary to establish the attorney-client privilege:
  - communication;
  - made in confidence;
  - to an attorney;
  - by a client;
  - for the purpose of seeking or obtaining primarily legal advice; and
  - not waived

Considerations:

- Circumstances when the attorney-client privilege is usually unavailable include:

  - When the privilege has been waived. The privilege belongs solely to the client and may only be waived by that client. A client waives the privilege by knowingly sharing the substance of a privileged communication between the client and the attorney with parties outside the privileged relationship. With respect to corporations, management has the authority to waive the privilege.

  - When the party asserting the privilege asserts a defense of advice-of-counsel. If a party asserts an advice-of-counsel defense, the party must waive the privilege, including testifying and/or producing documents, to the extent necessary to enable the staff to evaluate the validity of the defense. To assert a valid advice-of-counsel defense, courts have held that the defendant must establish that he or she (1) made complete disclosure to counsel; (2) requested counsel's advice as to the legality of the contemplated action; (3) received advice that it was legal; and (4) relied in good faith on that advice.

- Information that typically does not involve a confidential communication and therefore is not privileged include:

    - Identity of the client.
    - Existence of the attorney-client relationship.
    - General reason why the attorney was retained.
    - Fee arrangement between attorney and client.
    - Billing statements.

- Crime-fraud exception to attorney-client privilege: This is a rare exception. Most courts require the party wishing to invoke the crime-fraud exception to demonstrate that there is a factual basis for a showing of probable cause to believe that a crime or fraud has been committed and the communications in question were in furtherance of the crime or fraud. This burden is normally not met by showing that the communications in question might provide evidence of a crime or fraud but rather that the communication itself was in furtherance of the crime or fraud and was intended to facilitate or conceal the crime or fraud.

- Corporations asserting the attorney-client privilege: The attorney-client privilege can be asserted by a corporation to protect communications between corporate employees and in-house counsel. Courts have held that to assert the attorney-client privilege, a corporation must show that the communication came from a person who was employed with the corporation at the time of the communication, the employee was seeking legal advice from an attorney, and the communication was made within the scope of the employee's duties.

- Questions to consider asking to test the assertion of the attorney-client privilege include:

    - who prepared the document
    - who sent the document
    - to whom was the document sent
    - what was the date of the communication
    - what was the date on the document, or if none, the date the document was prepared, sent and/or received
    - who are the attorney and client involved
    - what was the nature of the document (*i.e.*, memorandum, letter, telegram, etc., and generic subject matter)
    - who are parties indicated on the document through carbon copy notations or

otherwise who were to receive the document, and all parties that in fact received or saw the document
- who was present during the communication
- who are the parties to whom the substance of the communication was conveyed
- would all of the communication, if disclosed to the staff, reveal or tend to reveal a communication from a client (made with the intention of confidentiality) to his/her attorney in connection with clients seeking legal services or legal advice at a time when the attorney was retained by that client
- would any segregable part of that communication not reveal or tend not to reveal such a confidential communication
- did a retention agreement between the attorney and client exist and if so, what is the date of such agreement
- during what period of time did the attorney-client relationship exist
- was a legal fee charged the client by the attorney in connection with the matter involving the communication; if so, how much, and how, when and by whom was it paid; if no fee was charged, was one discussed
- what was the general nature of legal services rendered, and during what time period
- did the communication primarily involve a business dealing between the attorney and client
- did the communication involve the client's seeking business advice
- was the communication a grant of authority or instruction for the attorney to act upon.

#### 4.1.1.1 Multiple Representations

Basics:

It is not unusual for counsel to represent more than one party (employees of the same company, for example).[7] Representing more than one party in an investigation does not necessarily present a conflict of interest, although it may heighten the potential for a conflict of interest.

**Considerations:**

When an attorney represents multiple parties, staff in testimony typically informs the party of what is contained in Form 1662, which states that:

> "You may be represented by counsel who also represents other persons involved in the Commission's investigation. This multiple representation, however, presents a potential conflict of interest if one client's interests are or may be

[7] Counsel is not precluded from representing more than one witness in the same investigation absent a showing that such representation will obstruct or impede the investigation. *See SEC v. Csapo*, 533 F.2d 7 (D.D.C. 1976); *see also SEC v. Higashi*, 359 F.2d 550 (9th Cir. 1966).

adverse to another's. If you are represented by counsel who also represents other persons involved in the investigation, the Commission will assume that you and counsel have discussed and resolved all issues concerning possible conflicts of interest. The choice of counsel, and the responsibility for that choice, is yours."

### 4.1.2 Attorney Work Product Doctrine

Basics:

- A party or the representing attorney may refuse to provide information on the basis that the information requested is protected by the attorney work product doctrine. If the documents or information requested were prepared in anticipation of litigation or for trial, or directly related to preparation for trial, then the work product doctrine generally applies and the party seeking discovery has the burden of proving substantial need and undue hardship. For material to be prepared in "anticipation of litigation," the prospect of litigation must be identifiable, although litigation need not have already commenced.

- Elements of the doctrine as set forth in Federal Rule of Civil Procedure 26(b)(3) are the following:

    - documents and tangible things
    - prepared in anticipation of litigation or for trial
    - by or for another party or by or for that party's representative, including attorney, consultant, surety, indemnitor, insurer, or agent
    - for which there is substantial need for the information and the information cannot be obtained elsewhere without undue hardship

Considerations:

- Voluntary disclosure of work product to the SEC generally constitutes a waiver.

- When a party asserts an advice-of-counsel defense, it must waive the attorney work product privilege to the extent necessary to enable the staff to evaluate the defense.

### 4.1.3 The Fifth Amendment Privilege Against Self-Incrimination

**Basics:**

- A witness testifying before the SEC may assert his or her Fifth Amendment privilege against self-incrimination.

- If a previous grant of immunity, or the expiration of the time limits for criminal prosecution prescribed by the statute of limitations, eliminates the danger of self-incrimination, the witness may not invoke the privilege.

**Considerations:**

- Staff typically will require testimony by or a declaration from the witness to assert the witness's Fifth Amendment privilege. Staff typically will not accept a letter from defense counsel as an alternative to testimony or a declaration.

    - Reasons for requiring a witness to appear in person to assert the Fifth Amendment privilege include, but are not limited to, obtaining a clear and specific privilege assertion on the record, allowing the staff to probe the scope of the privilege assertion, and allowing the staff to determine whether there are grounds to challenge the assertion.

    - A witness may not make a "blanket" assertion of the Fifth Amendment privilege.

    - In some cases, allowing assertion of the privilege by declaration may be more appropriate, for example, when time is of the essence.

- The Fifth Amendment privilege against self-incrimination protects individuals and sole proprietorships, but does not protect a collective entity, such as a corporation, or papers held by an individual in a representative capacity for a collective entity.

- Under the required records doctrine, the Fifth Amendment privilege against self-incrimination does not apply to records required to be kept by an individual under government regulation, such as tax returns.

- During litigation, the SEC can assert that an adverse inference should be drawn against a defendant who has asserted the Fifth Amendment privilege.

### 4.2 Inadvertent Production of Privileged or Non-Responsive Documents

Basics:

On September 19, 2008, the President signed S. 2450 into law, a bill adding new Evidence Rule 502 to the Federal Rules of Evidence. The new rule will apply in all proceedings commenced after the date of enactment and, insofar as is just and practicable, in all proceedings pending on such date of enactment. Under new Rule 502(b), when inadvertent disclosure is made to a federal agency, it does not operate as a waiver in a federal or state proceeding if a) the disclosure is inadvertent; b) the holder of the privilege took reasonable steps to prevent disclosure; and c) the holder promptly took reasonable steps to rectify the error.

If assigned staff receives inadvertently produced documents, assigned staff should promptly contact a supervisor at the Associate Director/Regional Office Head level or above and/or an Ethics liaison. Generally, staff will notify the party through his or her counsel of its receipt of inadvertently produced documents. Assigned staff should not

return a document to the party without prior consultation with his or her supervisor(s) and/or the Ethics Liaison.

Considerations:

- In determining how to respond after receiving a document that has been inadvertently produced, staff should consider when he or she was made aware of the production: prior to review of documents, upon review of documents, or after the review has been completed. In addition, staff should consider whether the documents are clearly privileged, possibly privileged, or simply nonresponsive.
- When assigned staff, in consultation with a supervisor and/or the Ethics liaison, determines that documents should be returned to the party, staff should require that the party create a privilege log.
- If assigned staff, along with his or her supervisors and/or the Ethics Liaison, determines that the staff has a legally sound and defensible basis for keeping the document, staff typically informs the party that staff possesses the document and intends to use it. Staff typically also informs the party whether and to whom staff has provided copies of the document outside the SEC (e.g., a judge or expert).
- If a document is not privileged, but is non-responsive, staff should consider whether the information may be useful as a basis for an inquiry or investigation, In addition, staff may want to alert other regulators or law enforcement authorities if staff discovers evidence of non-securities-related violations.

Further Information:

Assigned staff should refer any questions about this issue to their supervisors and to the Office of Chief Counsel.

### 4.2.1 Purposeful Production With No Privilege Review

Basics:

In some rare instances, a party may seek to produce documents and other responsive material to the staff before they have reviewed the material for privileged documents, and the party may seek to preserve any claims of privilege on these materials. In those circumstances, staff can choose to accept such a production in their case if they feel that it is to their benefit. Whether or not the staff chooses to accept such a production, the primary responsibility for identifying any privileged materials resides with the party, and acceptance is not an agreement to shift such responsibility to the staff. Further, the party must agree not to argue that the staff's investigation has been tainted by the staff's receipt, review, or examination of any material later determined to be privileged.

Considerations:

- In determining to accept such a production, staff should consider whether the acceptance will help to advance the staff's case by allowing the party to be able to provide the SEC with the requested production in a more expedited manner.

- If staff chooses to accept such a production, staff should clarify for the party that the staff will begin to look at the production immediately upon receipt, and that assigned staff will follow our regular procedures for handling inadvertent productions of privileged documents. For instance, assigned staff and their supervisors may decide that Enforcement has a legally sound and defensible basis for keeping a document that the party later claims as privileged. If this happens, staff should inform the party that Enforcement believes they have a basis for keeping the document.

- If a document is identified during the review as privileged or potentially privileged, and the party requests its return, staff should request that the party create a privilege log.

Further Information:

Assigned staff should refer any questions about this issue to their supervisors and to the Office of Chief Counsel.

### 4.3. Waiver of Privilege

Basics:

The staff must respect legitimate assertions of the attorney-client privilege and attorney work product protection, unless a party voluntarily chooses to waive privilege. As a matter of public policy, the SEC wants to encourage individuals, corporate officers and employees to consult counsel about potential violations of the securities laws.

A key objective in the staff's investigations is to obtain relevant information, and parties are, in fact, required to provide relevant information in response to SEC subpoenas. However, both entities and individuals may provide significant cooperation in investigations by *voluntarily* disclosing relevant information. That voluntary disclosure of information need not include a waiver of privilege to be an effective form of cooperation, as long as all relevant facts are disclosed.

The distinction between privileged communications or documents and unprivileged facts is often demonstrated in the course of a corporation's internal investigation regarding the conduct at issue in the staff's investigation. In corporate internal investigations, employees and other witnesses associated with a corporation are often interviewed by attorneys. If the interviews are conducted by attorneys, certain memoranda or notes generated in connection with the interview may be subject, at least in part, to the attorney-client or work product privileges. However, the underlying factual information disclosed by the witnesses during the interviews is not privileged.

***The staff should not ask a party to waive the attorney-client or work product privileges and is directed not to do so.*** All decisions regarding a potential waiver of privilege are to be reviewed with the Assistant supervising the matter and that review may involve more senior members of management as deemed necessary. The Enforcement Division's central concern is whether the party has disclosed all relevant facts within the party's knowledge that are responsive to the staff's information requests, and not whether a party has elected to assert or waive a privilege. As discussed below, if a party seeks cooperation credit for timely disclosure of relevant facts, the party must disclose all such facts within the party's knowledge. On request, and to the extent possible, the staff should continue to work with parties to explore alternative means of obtaining factual information when it appears that disclosure of responsive documents or other evidence may otherwise result in waiver of applicable privileges.

A party remains free to disclose privileged communications or documents if the party voluntarily chooses to do so. In this regard, the SEC does not view a party's waiver of privilege as an end in itself, but only as a means (where necessary) to provide relevant and sometimes critical information to the staff. In the event a party voluntarily waives privilege, the staff cannot assure the party that, as a legal matter, the information provided to the staff during the course of the staff's investigation will not be subject to disclosure pursuant to subpoena or other legal process.

Considerations:

- The SEC encourages and rewards cooperation by parties in connection with staff's investigations. One important measure of cooperation is whether the party has timely disclosed facts relevant to the investigation. Other measures of cooperation include, for example, voluntary production of relevant factual information the staff did not directly request and otherwise might not have uncovered; requesting that corporate employees cooperate with the staff and making all reasonable efforts to secure such cooperation; making witnesses available for interviews when it might otherwise be difficult or impossible for the staff to interview the witnesses; and assisting in the interpretation of complex business records. The SEC's policy with respect to cooperation is set forth in the Seaboard 21(a) Report, Sec. Rel. No. 44969 n.3 (Oct. 23, 2001), which outlines other numerous factors that may be considered in assessing whether to award credit for cooperation.

- Waiver of a privilege is not a pre-requisite to obtaining credit for cooperation. A party's decision to assert a legitimate privilege will not negatively affect their claim to credit for cooperation. The appropriate inquiry in this regard is whether, notwithstanding a legitimate claim of privilege, the party has disclosed all relevant underlying facts within its knowledge.

- By timely disclosing the relevant underlying facts, a party may demonstrate cooperation for which the staff may give credit, while simultaneously asserting privilege. The timely disclosure of relevant facts is considered along with all other cooperative efforts and circumstances in determining whether and the extent to which the party should be awarded credit for cooperation. *See id.*

Exceptions re Assertion of Privileges:

- In order to rely on advice-of-counsel as a defense, a party must waive the attorney-client privilege and work product protection to the extent necessary to enable the staff to evaluate the defense. Staff at the Assistant Director level or higher should attempt to explore the possibility of an advice-of-counsel defense with a party's counsel at an early stage in the investigation. It is important to obtain all relevant documents and testimony at the earliest possible date.

- Staff should consider whether there may be other circumstances that negate assertions of privilege, such as the crime-fraud exception and prior non-privileged disclosure. These and other such circumstances should be considered in analyzing the legitimacy of a party's assertion of privilege.

Further Information:

- For more information on the attorney-client and work product privileges, and exceptions thereto, please consult Sections 4.1.1 (Attorney-Client Privilege) and 4.1.2 (Attorney Work Product Doctrine) of the Manual.
- For information on the inadvertent production of privileged materials, please consult Section 4.2 of the Manual.
- For information on the production of privileged materials pursuant to a Confidentiality Agreement, please consult Section 4.3.1 of the Manual.

### 4.3.1 Confidentiality Agreements

Basics:

A confidentiality agreement is an agreement between the staff of the Division of Enforcement and, typically, a company subject to investigation pursuant to which the company agrees to produce materials that it considers to be privileged (such as reports of an internal investigations, interview memoranda, and investigative working papers). For its part, the staff agrees not to assert that the entity has waived any privileges or attorney work-product protection by producing the documents. The staff also agrees to maintain the confidentiality of the materials, except to the extent that the staff determines that disclosure is required by law or that disclosure would be in furtherance of the SEC's discharge of its duties and responsibilities. The basis for the agreement is the interest of

the staff in determining whether violations of the federal securities laws have occurred, and the company's interest in investigating and analyzing the circumstances and people involved in the events at issue.

Considerations:

- The Division typically uses a Model Confidentiality Agreement (below), and the staff should not agree to modifications to the Model Confidentiality Agreement without first consulting with the Office of Chief Counsel and/or the Head of the Trial Unit. The agreement must be signed by a supervisor at or above the level of an Assistant Director.
- While obtaining materials that are otherwise potentially subject to privilege or the protections of the attorney work-product doctrine can be of substantial assistance in conducting an investigation, the staff should exercise judgment when deciding whether to enter into a confidentiality agreement with a company under investigation. Considerations include the following:
    - Some courts have held that companies that produce otherwise privileged materials to the SEC or the U.S. Department of Justice, even pursuant to a confidentiality agreement, waived privilege in doing so.
    - Some companies have important pertinent operations in one or more foreign jurisdictions, which may have data privacy and other laws that will restrict the staff's ability to obtain evidence. The company itself may have access to the persons in such jurisdictions (especially if they are still employees) and to other sources of evidence (such as documents and e-mails). In such instances, the company may be able to convey important information to the staff by producing interview memoranda and through reports of findings derived from otherwise restricted sources.

Model Confidentiality Agreement:

[**date**]

[**SEC address**]

Re: In the Matter of [**investigation name and number**]

Dear Mr./Ms. [**name**]:

The [**name**] Committee of [**company**] commenced a [**review or investigation**] of [**issue**] on or about [**date**]. The [**name**] Committee has prepared a report, interview memoranda and investigative working papers in connection with this [**review or investigation**]. In light of the interest of the Staff of the U.S. Securities and Exchange Commission (the "Staff") in determining whether there have been any violations of the federal securities laws, and the [**name**] Committee's interests in investigating and analyzing the circumstances and people involved in the events at issue, the [**name**] Committee will provide to the Staff copies of the report, interview memoranda and investigative working papers [**, in addition to oral briefings**] ("Confidential Materials").

Please be advised that by producing the Confidential Materials pursuant to this agreement, the [**name**] Committee does not intend to waive the protection of the attorney work product doctrine, attorney-client privilege, or any other privilege applicable as to third parties. The [**name**] Committee believes that the Confidential Materials are protected by, at a minimum, the attorney work product doctrine and the attorney-client privilege. The [**name**] Committee believes that the Confidential Materials warrant protection from disclosure.

The Staff will maintain the confidentiality of the Confidential Materials pursuant to this agreement and will not disclose them to any third party, except to the extent that the Staff determines that disclosure is otherwise required by law or would be in furtherance of the Commission's discharge of its duties and responsibilities.

The Staff will not assert that the [**name**] Committee's production of the Confidential Materials to the Commission constitutes a waiver of the protection of the attorney work product doctrine, the attorney-client privilege, or any other privilege applicable as to any third party. The Staff agrees that production of the Confidential Materials provides the Staff with no additional grounds to subpoena testimony, documents or other privileged materials from the [**name**] Committee, although any such grounds that may exist apart from such production shall remain unaffected by this agreement.

The Staff's agreement to the terms of this letter is signified by your signature on the line provided below.

Sincerely,

_____
Chair of the [**name**] Committee of
[**company**]

AGREED AND ACCEPTED:
United States Securities and Exchange Commission

By: _____
Division of Enforcement

### 4.4 Compliance with the Privacy Act

Basics:

- The Privacy Act of 1974, 5 U.S.C. Section 552a, establishes requirements for the solicitation and maintenance by agencies of personal information regarding members of the public.

- When obtaining information from the public, the statute requires the staff to provide notice with respect to the authority for the solicitation and whether disclosure is voluntary or mandatory; the principal purposes for seeking the information; the effect of refusing to provide the information; and the "routine uses" of the information. The statute prohibits any disclosure of personal information unless the disclosure is within one of the statute's exemptions (including the exemption for "routine uses"). In addition, the statute requires that agencies have the ability to account for disclosures.

Considerations:

The Privacy Notice requirement is generally met by providing a copy of Form 1661 or Form 1662 to the person or entity from whom information is sought. The forms contain the list of uses that may be made of personal information. Generally, disclosures in aid of the staff's investigations will be covered by one or more of the routine uses.

Further Information:

- For questions relating to the Privacy Act, please contact the Office of Chief Counsel.

- For further information on Forms 1661 and 1662, please see Section 3.2.3.1 of the Manual.

- For further information on how to meet the Privacy Act requirements when conducting voluntary telephone interviews, please see 3.3.3.1 of the Manual.

### 4.5 Compliance with the Right to Financial Privacy Act ("RFPA")

Basics:

- The Right to Financial Privacy Act of 1978 (12 U.S.C. Sections 3401 – 3422) provides individuals with a privacy interest in their banking records held by a financial institution. Section 21(h) of the Exchange Act contains additional RFPA procedures available only to the SEC.

- The RFPA applies when staff seeks the financial records of a "customer" (*i.e.*, an individual or partnership of five or fewer individuals) from a "financial institution" (*e.g.*, a bank, mortgage lending company or trust company, but not regulated entities, such as broker-dealers or investment advisers). Generally, the staff may only obtain customer records from a financial institution pursuant to subpoena, after providing the customer with notice of the subpoena and an opportunity to challenge production in court. Notice must also be provided when the staff discloses information obtained pursuant to the RFPA to another federal agency (absent an exemption, such as that for disclosure to the Department of Justice).

Considerations:

- The staff should be aware of RFPA restrictions whenever seeking banking records, including those of non-customers, to avoid inadvertent non-compliance. In situations where notice to the customer may impede an investigation or result in the movement of funds out of U.S. jurisdiction, staff may consider seeking a court order under Section 21(h) of the Exchange Act to delay notice; the staff may also consider filing an emergency action to obtain a freeze order to protect investor funds.

- The staff should also be aware of RFPA restrictions whenever disclosing information obtained from a financial institution to another federal agency.

Further Information:

For further information about the RFPA and its requirements, please contact the Office of Chief Counsel.

### 4.6 Compliance with the Electronic Communications Privacy Act ("ECPA")

Basics:

- The Electronic Communications Privacy Act of 1986 ("ECPA"), 18 U.S.C. Sections 2510 – 2711, expanded the wiretap laws to protect the contents of electronic communications (*e.g.*, e-mail) in the hands of third-party electronic communications service providers.

- A government agency can obtain communications that have been held by a third-party service provider for more than 180 days pursuant to subpoena; the agency must provide notice of the subpoena to the customer. (E-mail service providers rarely retain message contents for this length of time.) The content of communications held by a third-party service provider for less than 180 days may only be obtained by criminal law enforcement authorities pursuant to warrant; staff should consult with the Office of Internet Enforcement regarding preservation of e-mail content held for less than 180 days.

- The statute also authorizes agencies to obtain telephone records and e-mail records (other than content) by subpoena. This information will include the name, address, local and long distance telephone connection records, or records of session times and durations; length of service (including start date) and types of service utilized; telephone or instrument number or other subscriber number or identity, including any temporarily assigned network address; and the means and source of payment for such service (including any credit card or bank account number). No customer notice is required when obtaining such records.

Considerations:

- The staff should be aware of ECPA restrictions whenever seeking information or records from persons who provide computerized communication services to the public. These service providers include online information services, national and local entities that permit customers to gain access to the Internet, and any other person that permits customers to communicate via e-mail or bulletin boards. Access to information and records from any of these entities may be subject to the ECPA.

- All requests for information from service providers (except telephone companies when seeking telephone records) must be coordinated with the Division's Office of Internet Enforcement.

- The ECPA applies only to records held by third-party service providers, and hence does not apply to e-mail held by the sender or addressee, or held on the servers of a company that provides internal e-mail services for its own employees.

- As a result of changes in the language of Section 2703 of the ECPA, and in telephone billing practices, service providers have increasingly submitted requests for reimbursement for production of transactional records regarding telephone and electronic communication services. The staff continues to believe that such reimbursement was not contemplated at the time the statute was enacted; however, reasonable invoices submitted after compliance with staff subpoenas may be considered. Assigned staff should consult with their supervisors and the Office of Internet Enforcement if they receive a request for reimbursement.

Further Information:

For further information on whether the ECPA may apply and the procedures to follow when it does, please consult the Office of Internet Enforcement and the Office of Chief Counsel.

### 4.7 Handling Materials from FinCEN or Other Sources Involving Bank Secrecy Act Material

Introduction:

The Bank Secrecy Act ("BSA") was enacted in 1970 and amended by the USA PATRIOT Act. It is designed to prevent financial institutions, including broker-dealers, from being used as vehicles to hide the transfer of illegally obtained funds. The BSA is codified at 31 U.S.C. Section 5311, *et seq*. The regulations implementing the BSA are located at 31 C.F.R. Part 103.

For the SEC, the primary mechanism for enforcing compliance by brokers and dealers with the requirements of the BSA is Section 17(a) of the Exchange Act and Rule 17a-8. In the investment company context, the relevant rule is Rule 38a-1 of the ICA.

Basics:

- The Financial Crimes Enforcement Network ("FinCEN") has determined that BSA materials are non-public documents and that, absent certain circumstances, these materials are privileged documents. Absent certain circumstances, staff is restricted by law from disseminating BSA material in litigation or to the public. However, staff may use the information contained in the BSA material as a lead to possible *underlying* documents of value in an investigation. All hardcopy BSA material should be segregated and kept under lock and key or if in electronic form, in a secure electronic file.

- BSA material may include, among other documents, Suspicious Activity Reports ("SARs"); Currency Transaction Reports ("CTRs") and Currency Transaction Reports by Casinos ("CTRCs") (i.e., reports on transactions in excess of $10,000); Reports of Foreign Bank and Financial Interests ("FBARs"); Reports of International

Transportation of Currency or Monetary Instruments ("CMIRs"); and Reports of Cash Payments Over $10,000 Received in Trade or Business.

Considerations:

- Staff is permitted to share the information contained in BSA material with other SEC staff if relevant to an inquiry or investigation. Staff should not make copies or forward electronic copies of BSA information, particularly SARs, which are highly sensitive documents. Staff generally should not disclose BSA information or its existence to persons who may be assisting in a matter, such as an Independent Compliance Person, or Receiver because BSA materials are non-public documents. BSA materials cannot be shown to witnesses or marked as exhibits in testimony.

- Please keep in mind that BSA materials may be embedded within a document production. Therefore, staff should add the following language to letter requests for documents to regulated entities and to subpoenas to financial institutions:

  **"If the document production contains Bank Secrecy Act materials, please segregate and label those materials within the production."**

Further information:

- Staff should contact the Office of Chief Counsel for further information about how to handle BSA materials received from FinCEN or other sources.

- *See also* Section 2.2.2.1 of the Manual.

## 5. Cooperation with Other Agencies and Organizations

### 5.1 Disclosure of Information and Access Requests

Basics:

All information obtained or generated by SEC staff during investigations or examinations should be presumed confidential and nonpublic unless disclosure has been specifically authorized. The SEC's rules permit the staff, by delegated authority, to grant access to nonpublic information to domestic and foreign governmental authorities, self-regulatory organizations, and other specified persons. Disclosures of such information to members of the general public will normally be made only pursuant to the Freedom of Information Act.

Rule 2: The "Discussion Rule":

Cooperation and coordination with other law enforcement agencies often require the staff to engage in discussions of nonpublic information prior to the grant of a formal access request. Rule 2 of the SEC's Rules Relating to Investigations was adopted to permit discussions with those persons who may obtain access to nonpublic information through the SEC's access program. Discussions under Rule 2 must be authorized by officials at or above the level of Assistant Director. Rule 2 extends only to the conduct of discussions and not to the furnishing of nonpublic documents. *See* Rule 2 of the SEC's Rules Relating to Investigations, 17 C.F.R. Section 203.2.

The Access Program:

Section 24(c) of the Exchange Act and Rule 24c-1 authorize the SEC to grant access to nonpublic information in enforcement files. Note, however, that work product and other privileged information is rarely disclosed, even when third-parties are granted access to the other materials in nonpublic files, and should not be disclosed without specific supervisory approval.

Rule 24c-1 authorizes disclosure to the following classes of requestors:

- Federal, state, local and foreign governmental authorities;
- self-regulatory and similar organizations;
- foreign financial regulatory authorities;
- SIPC and SIPC trustees;
- trustees in bankruptcy;
- court-appointed counsel, and similar persons, charged with performing functions arising from securities litigation (e.g., as receivers or trustees of disgorgement funds);
- professional licensing or oversight authorities (e.g., bar associations created by the courts); and
- agents, employees or representatives of such persons.

Access Procedures:

The SEC's rules require that all access requests be in writing and signed by an official who is in a sufficiently senior or supervisory position to make and enforce required representations. Requestors are generally expected to use the Division's form access letters.

An access recommendation form must be signed by a recommending staff member who is a supervisor at or above the SK-16 level. The recommendation form (and a copy of the incoming request) is then forwarded to an SEC official authorized to approve the request. The Director of the Division of Enforcement has been delegated authority to grant requests, and this authority has been sub delegated to certain senior staff.

When an access request has been approved, the appropriate letter is sent to the requestor, and documents covered by the access grant may then be disclosed.

Further Information:

For further information regarding the access program and procedures, please consult with the Office of Chief Counsel.

### 5.2 Cooperation with Criminal Authorities

Cooperating with criminal authorities is an important component of the SEC's enforcement mission. The SEC is an independent federal agency charged by Congress with upholding the federal securities laws. The SEC has independent authority to bring civil, but not criminal, actions to enforce those laws. This authority is not compromised when the Department of Justice or state criminal authorities conduct a criminal investigation and/or make a determination to bring criminal charges concurrent with the SEC's investigation and/or civil action. Nonetheless, there are certain unique considerations that arise when cooperating with criminal authorities, as discussed in Sections 5.2.1 and 5.2.2 of the Manual.

### 5.2.1 Parallel Investigations

Basics:

Parallel civil and criminal proceedings are not uncommon.[8] In furtherance of the SEC's mission and as a matter of public policy, the staff is encouraged to work cooperatively with criminal authorities, to share information, and to coordinate their investigations with parallel criminal investigations when appropriate. There are, however, a number of considerations the staff should be mindful of when conducting a parallel investigation and when determining whether to seek authorization to bring a case that involves a parallel criminal investigation. Because each case presents a unique set of circumstances, assigned staff should consult with supervisors whenever they are involved in parallel proceedings.

Considerations:

While every situation is different, the staff typically should keep the following considerations in mind when conducting a parallel investigation and when determining whether to seek authorization to bring a case that involves a parallel criminal investigation:

- It is important that the civil investigation has its own independent civil investigative purpose and not be initiated to obtain evidence for a criminal prosecution. This does not prevent the staff from taking an action simply because the action will benefit not only the SEC investigation, but also a criminal investigation. It does mean, however, that staff should not take an SEC civil investigative action for which the *sole* aim is to benefit the criminal authorities.

- The staff should make its own independent decision about what documents to request, what investigative testimony to take, what questions to ask during testimony, the location of testimony and similar matters.

[8] The Supreme Court recognized in *United States v. Kordel*, 397 U.S. 1, 11 (1970) that parallel civil and criminal proceedings are appropriate and constitutional. As the Court of Appeals for the D.C. Circuit put it in the leading case of *SEC v. Dresser*, 628 F.2d 1368, 1377 (D.C. Cir. 1980), "effective enforcement of the securities laws require that the SEC and [the Department of] Justice be able to investigate possible violations simultaneously." Other courts have issued opinions to the same effect. *E.g., SEC v. First Financial Group of Texas*, 659 F.2d 660, 666-67 (5th Cir. 1981) ("The simultaneous prosecution of civil and criminal actions is generally unobjectionable."); *United States v. Stringer*, 521 F.3d 1189, 1191 (9th Cir. 2008) *(*"There is nothing improper about the government undertaking simultaneous criminal and civil investigations. . ."*).* Moreover, the federal securities laws themselves expressly provide that the SEC can share information gathered in a civil investigation with other government agencies and provide information to the Department of Justice for a determination whether to institute criminal proceedings. *See* Section 20(b), Securities Act; Section 21(d), Exchange Act; 17 C.F.R. § 240.24c-1 (access to nonpublic information).

- If asked by counsel or any individual whether there is a parallel criminal investigation, staff should direct counsel or the individual to the section of Form 1662 dealing with "Routine Uses of Information[9]," and state that it is the general policy of the Commission not to comment on investigations conducted by law enforcement authorities responsible with enforcing criminal laws. Staff should also invite any person who raises such issues to contact criminal authorities if they wish to pursue the question of whether there is a parallel criminal investigation. Should counsel or the individual ask which criminal authorities they should contact, staff should decline to answer unless authorized by the relevant criminal authorities.

- Supervisors must be involved in all significant discussions and written communications with criminal authorities.

- Generally, sharing information with criminal prosecutors is permissible, even though the sharing of information is intended to and does in fact assist criminal prosecutors. In addition, in certain circumstances it is appropriate for criminal authorities to ask SEC staff to refrain from taking actions that would harm the criminal investigations, and likewise it can be appropriate for SEC staff to ask criminal authorities not to take action that would harm our investigations. Each case is unique and assigned staff should discuss these and other considerations with their supervisors.

Further Information:

- For more information regarding the "Discussion Rule" and access requests, see Section 5.1 of the Manual.

- For more information on joint proffer sessions, see Section 3.3.5.4 of the Manual.

### 5.2.2 Grand Jury Matter

Basics:

The SEC is generally not privy to grand jury matter. Grand jury matter is subject to the confidentiality restrictions set forth in Federal Rule of Criminal Procedure 6(e) and

[9] This section of Form 1662 states that "The Commission often makes its files available to other government agencies, particularly United States Attorneys and state prosecutors. There is a likelihood that information supplied by you will be made available to such agencies where appropriate. Whether or not the Commission makes its files available to other government agencies is, in general, a confidential matter between the Commission and such governmental agencies."

analogous state rules of criminal procedure. Rule 6(e) provides for secrecy of all "matter(s) occurring before the grand jury," subject to certain exceptions.

Considerations:

- Subject to the limitations in Rule 6(e) and similar state rules, the staff is allowed to receive information from the criminal authorities about the status of the criminal investigation and the future investigative plans of the criminal authorities.

- Before receiving information from the criminal authorities in an investigation, staff should inquire whether any of the information provided comes directly or indirectly from grand jury proceedings, including subpoenas.

- If assigned staff comes into possession of grand jury matter, he or she should immediately inform his or her supervisor in order to take appropriate steps.

### 5.3 Cooperation with the Food and Drug Administration ('FDA")

Authority:

- Section 331(j) of the Federal Food, Drug and Cosmetic Act prohibits the FDA from disclosing trade secrets, even to other federal agencies such as the SEC.

- 21 C.F.R. Section 20.85 allows the FDA to share other nonpublic records with other federal agencies, but before disclosing such information the FDA must receive a written agreement that the information will not be further disclosed by the other agency without written permission from the FDA.

- The FDA will not agree to further disclosure of confidential commercial information without the consent of the owner or submitter of the information.

- Before the FDA will grant permission for any further disclosure, the agency will review each document to identify potentially privileged or otherwise protected information.

- The FDA Commissioner must authorize any investigative testimony by FDA employees (21 C.F.R. Section 20.1(c)).

Basics:

Staff may seek information from the FDA in investigations arising from referrals by the FDA, or in which the FDA may have relevant information. (For example, a company's public statements about the status for FDA approval of its product may cause the staff to seek information from the FDA about its review of the product.) Before making any request to the FDA, staff should review the statutes and regulations that

govern the FDA's ability to disclose information to SEC staff. Assigned staff should also consult with their supervisors about the scope of the request and the appropriate addressee. The designated Enforcement Division FDA liaison should be informed of requests.

To obtain non-public information or records, staff can prepare a written request, including:

- identification of the type of information requested,
- whether the request is the result of an ongoing investigation,
- the purpose for which the information is requested,
- acknowledgement that trade secret information cannot be disclosed,
- agreement to protect the confidentiality of non-public information received,
- agreement not to further disclose the non-public information without written consent from the FDA.

The written request should be addressed to an appropriate FDA contact person.

To obtain investigative testimony from an FDA employee, staff can prepare a written request, including:

- identification of the employee whose testimony is sought,
- a description of the subject matter of the investigation,
- the subject matter of the requested testimony,
- how the testimony would serve the public interest and promote the interests of the FDA.

The written request should be addressed to the Commissioner of the FDA. Before requesting testimony from an FDA employee, staff should contact the appropriate FDA lawyer.

To request FDA permission to make further disclosure of non-public records or information the FDA has provided to SEC staff, staff can prepare a written request and make a set of the documents or transcripts it wishes to disclose, to attach to the request.

Considerations:

Documents relating to FDA consideration of applications for new drugs or biologics can be extremely voluminous—sometimes millions of pages—so staff should consider the extent to which they are relevant to its investigation before making broad requests for all documents relating to a product.

When preparing to litigate a case in which non-public FDA documents or testimony transcripts will be part of the SEC's initial disclosure, staff should keep in mind that before the FDA consents to further disclosure, it will conduct a review of each page to determine whether any of the material is privileged. Because this review can take

a very long time, staff should allow ample time for that review before filing a case or in the litigation discovery schedule.

If staff expects to charge a defendant who is not the owner of the information (for example, a current or former employee of the company), staff should seek consent from the company for the disclosure as early as practical, because the FDA will not agree to further disclosure of confidential commercial information without the consent of the owner or submitter of the information.

Further information:

- Please refer any questions about FDA matters to the designated Enforcement Division liaison or the Office of Chief Counsel.

- For more information on the FDA, see Inside the FDA, a manual available on the FDA's public website, www.fda.gov .

### 5.4 Cooperation with the Public Company Accounting Oversight Board ("PCAOB")

Basics:

The SEC and the PCAOB have a mutual interest in ensuring that investigations relating to the audit profession are properly coordinated. This will help to promote, among other things, consistent regulatory approaches as well as efficient and cost effective investigations and enforcement actions.

Considerations:

- The SEC and PCAOB generally have concurrent jurisdiction over auditors but there may be instances in which it may be preferable for one organization to be principally responsible for investigating an auditor's conduct.

- Some of the factors the staff may wish to evaluate when coordinating investigations with the PCAOB include differences between charges and remedies, the nature of the conduct, and the standards involved.

### 5.5 Informal Referrals from Enforcement

Introduction:

The staff may informally refer a matter to federal or state criminal authorities, self-regulatory organizations, the Public Company Accounting Oversight Board, or state agencies. The decision to make an informal referral should be made in the Home Office by officials at or above the level of Associate Director. In the Regional Offices, the

decision to make an informal referral should be made by an official at or above the level of Regional Head of Enforcement.

The staff may also determine that it is appropriate to refer a matter or information concerning potential professional misconduct to state bar associations or other state professional associations. Such referrals, however, are considered Commission actions and the staff must follow the procedures described in Section 5.5.5 of the Manual.

Authority:

A number of SEC rules grant the staff the authority to make informal referrals.

- **Rule 5(b) of the SEC's Informal and Other Procedures, 17 C.F.R. Section 202.5(b):**

  After investigation or otherwise the Commission may in its discretion take one or more of the following actions: Institution of administrative proceedings looking to the imposition of remedial sanctions, initiation of injunctive proceedings in the courts, and, in the case of a willful violation, reference of the matter to the Department of Justice for criminal prosecution. The Commission may also, on some occasions, refer the matter to, or grant requests for access to its files made by, domestic and foreign governmental authorities or foreign securities authorities, self-regulatory organizations such as stock exchanges or the National Association of Securities Dealers, Inc., and other persons or entities.

- **Rule 2 of the SEC's Rules Relating to Investigations, 17 C.F.R. Section 203.2:**

  Information or documents obtained by the Commission in the course of any investigation or examination, unless made a matter of public record, shall be deemed non-public, but the Commission approves the practice whereby officials of the Divisions of Enforcement, Corporation Finance, Trading and Markets, and Investment Management and the Office of International Affairs at the level of Assistant Director or higher, and officials in Regional Offices at the level of Assistant Regional Director or District Administrator or higher, may engage in and may authorize members of the Commission's staff to engage in discussions with persons identified in Section 240.24c-1(b) of this chapter concerning information obtained in individual investigations or examinations, including formal investigations conducted pursuant to Commission order.

- **Rule 24c-1(b) of the Exchange Act, 17 C.F.R. Section 240.24c-1(b):**

  The Commission may, in its discretion and upon a showing that such information is needed, provide nonpublic information in its possession to any of the following persons if the person receiving such nonpublic information provides such assurances of confidentiality as the Commission deems appropriate:

(1) A federal, state, local or foreign government or any political subdivision, authority, agency or instrumentality of such government;
(2) A self-regulatory organization as defined in Section 3(a)(26) of the Act, or any similar organization empowered with self-regulatory responsibilities under the federal securities laws (as defined in Section 3(a)(47) of the Act), the Commodity Exchange Act (7 U.S.C. Section 1, et seq.), or any substantially equivalent foreign statute or regulation;
(3) A foreign financial regulatory authority as defined in Section 3(a)(51) of the Act;
(4) The Securities Investor Protection Corporation or any trustee or counsel for a trustee appointed pursuant to Section 5(b) of the Securities Investor Protection Act of 1970;
(5) A trustee in bankruptcy;
(6) A trustee, receiver, master, special counsel or other person that is appointed by a court of competent jurisdiction or as a result of an agreement between the parties in connection with litigation or an administrative proceeding involving allegations of violations of the securities laws (as defined in Section 3(a)(47) of the Act) or the Commission's Rules of Practice, 17 CFR Part 201, or otherwise, where such trustee, receiver, master, special counsel or other person is specifically designated to perform particular functions with respect to, or as a result of, the litigation or proceeding or in connection with the administration and enforcement by the Commission of the federal securities laws or the Commission's Rules of Practice;
(7) A bar association, state accountancy board or other federal, state, local or foreign licensing or oversight authority, or a professional association or self-regulatory authority to the extent that it performs similar functions; or
(8) A duly authorized agent, employee or representative of any of the above persons.

### 5.5.1 Informal Referrals to Criminal Authorities

Basics:

Staff inquiries or investigations may reveal conduct that warrants informal referral to criminal law enforcement authorities – including federal, state or foreign criminal law enforcement authorities. If there is a matter or conduct that appears to warrant an informal referral, staff generally should follow the procedures below:

- Assigned staff should consult with their direct supervisors and obtain approval at the Associate Director or Regional Head of Enforcement level to informally refer the matter or conduct. Informal referrals to foreign criminal authorities should also first be discussed with the Office of International Affairs so that consideration is given to policies and procedures of the foreign authorities.

- Once Associate or Regional Head of Enforcement approval has been obtained, assigned staff along with their supervisors may notify the appropriate criminal authorities.

- Staff may then invite the criminal authorities to make an access request (see Section 5.1 regarding access requests). When the access request has been approved, staff may share documents from the investigative file. Staff may not forward documents to the criminal authorities prior to the approval of the access request.

- After an informal referral to criminal authorities is made, staff is encouraged to maintain periodic communication with the criminal authorities concerning the status of any criminal investigation. See Section 5.2 of the Manual for information relating to parallel investigations, the grand jury secrecy rule, and other concerns when cooperating with criminal authorities.

Considerations:

- In determining whether to make an informal referral to criminal law enforcement authorities, the staff may consider, among other things, the egregiousness of the conduct, whether recidivism is a factor, and whether the involvement of criminal authorities will provide additional meaningful protection to investors.

- In determining whether to make an informal referral to federal, state, or foreign criminal authorities, the staff may also consider jurisdictional factors, such as where the conduct occurred or the domicile of the possible violators.

### 5.5.2 Informal Referrals to Self Regulatory Organizations ("SROs")

Basics:

In the course of conducting an inquiry or investigation, the staff may determine that it would be appropriate to informally refer the matter, or certain conduct, to one or more self-regulatory organizations ("SROs"). In particular, if an inquiry or investigation concerns matters over which SROs have enforcement authority (*e.g.*, financial industry standards, rules and requirements related to securities trading and brokerage), staff should evaluate whether to contact the SRO about the matter and assess whether it would be appropriate for the SRO to consider investigating the matter in lieu of, or in addition to, an SEC Enforcement investigation. Because SROs may impose disciplinary or remedial sanctions against their members or associated individuals, staff generally should make an effort to apprise the SRO about conduct that may violate the rules of the SRO. Internally, staff generally should consult with the Office of Market Surveillance and the Division of Trading and Markets in evaluating potential informal referrals to SROs.

If there is a matter or conduct that appears to warrant an informal referral, staff generally should follow the procedures below:

- Assigned staff should consult initially with their direct supervisors, as well as the Office of Market Surveillance and the Division of Trading and Markets, as appropriate.

- Assigned staff must obtain approval at the Associate Director or Regional Head of Enforcement level to informally refer the matter or conduct.

- Once approval has been obtained, assigned staff along with their supervisors may notify the appropriate liaison at the SRO to discuss the matter and/or conduct, and a possible informal referral.

- Staff may then invite the SRO to make an access request (*see* Section 5.1 of the Manual regarding access requests). When the access request has been approved, staff may share documents from the investigative file. Staff may not forward documents to the SRO prior to the approval of the access request.

- After an informal referral to an SRO is made, staff should maintain periodic communication with the SRO concerning the status of the SRO inquiry or investigation and periodically assess whether any or additional SEC Enforcement measures should be taken.

Considerations:

Staff should be mindful of the following considerations when making or considering an informal referral to an SRO:

- In the early stages of an inquiry or investigation, staff should consider evaluating whether an informal referral is warranted. As the investigation progresses, the staff are encouraged to periodically review the record to determine whether a new or additional informal referral may be appropriate.

- Staff should make efforts to continue communication with SRO staff throughout the SRO's inquiry or investigation to ensure that SEC staff and SRO staff are not investigating the same conduct, and so that SEC staff is aware of any determination by SRO not to pursue an investigation or certain avenues of investigation.

Further information:

- Please refer any questions about making an informal referral to an SRO to supervisors and/or the Office of Market Surveillance.

- For guidance regarding receiving referrals *from* an SRO, see Section 2.2.2.5 of the Manual.

### 5.5.3 Informal Referrals to the Public Company Accounting Oversight Board ("PCAOB")

Basics:

In certain instances, Enforcement staff may informally refer matters regarding auditor misconduct to the Public Company Accounting Oversight Board ("PCAOB"), which is authorized, under Section 105 of the Sarbanes-Oxley Act, to conduct investigations, and impose disciplinary or remedial sanctions against public accounting firms and their associated persons. If there is a matter that may be appropriate for referral, assigned staff generally should follow the procedures below:

- Assigned staff should consult initially with their supervisors.
- Assigned staff should then get approval at or above the Associate Director or Regional Head of Enforcement level to refer the matter.
- Assigned staff should then discuss the matter with the Chief Accountant of Enforcement, and secure his or her approval for making the referral.
- Assigned staff should then, along with their supervisor, or through the office of Enforcement's Chief Accountant, call the head of enforcement, or another designated official, at the PCAOB, and discuss the matter.
- Staff can then invite the PCAOB to make an access request (see Section 5.1). Once the access request has been approved, staff can share documents from the investigative file. Staff should provide a copy of the access request to the Chief Accountant of Enforcement.

Considerations:

Please keep in mind the following considerations when making a referral to the PCAOB:

- How old is the conduct? PCAOB typically has jurisdiction from October 2003 forward for U.S. audit firms, and July 2004 for foreign audit firms.
- Staff should consider evaluating whether to refer a matter as early as the inception of an investigation, and in any event, as the investigation progresses.
- Staff should continue communication with PCAOB staff throughout the PCAOB's investigation, so that SEC staff and PCAOB staff are not investigating the same conduct, and also so that SEC staff are alerted to any determination by the PCAOB not to pursue its investigation.

Further Information:

- Please refer any questions about making an informal referral to the PCAOB to the Chief Accountant of the Enforcement Division.

- For guidance regarding receiving tips from the PCAOB, see Section 2.2.2.2 of the Manual.

### 5.5.4 Informal Referrals to State Agencies

Basics:

Congress created a dual securities regulatory system in which both federal and state agencies serve specific, valuable functions in protecting investors. In the course of conducting an informal inquiry or formal investigation, the staff may determine that it would be appropriate to informally refer the matter, or certain conduct, to state regulators. It may be appropriate for the state agency to investigate the matter in lieu of, or in addition to, an SEC Enforcement investigation.

If there is a matter or conduct that appears to warrant an informal referral, staff generally should follow the procedures below:

- Assigned staff should consult with their direct supervisors and obtain approval at the Associate Director or Regional Head of Enforcement level to informally refer the matter or conduct.

- Once approval has been obtained, assigned staff along with their supervisors may contact the state agency and discuss with them the relevant findings of the inquiry or investigation to date and explain why the staff is informally referring the matter.

- Staff may then invite the state agency to make an access request (see Section 5.1 regarding access requests). When the access request has been approved, staff may share documents from the investigative file. Staff may not forward documents to the state agency prior to the approval of the access request.

Considerations:

Assigned staff should discuss with their supervisors whether it may be appropriate to informally refer a matter or certain conduct to the state. For example, a state may have a particular interest in a case or type of case, the victims or parties may be concentrated in a particular geographic location, the conduct or amount of losses may be limited, though significant, or there may be no federal jurisdiction. In the early stages of an inquiry or investigation, staff should evaluate whether an informal referral is warranted. As the investigation progresses, the staff is encouraged to periodically review the record to determine whether a new or additional informal referral may be appropriate. Staff is also

encouraged to continue communication with the state agency after an informal referral has been made.

### 5.5.5 Informal Referrals to Professional Licensing Boards

Basics:

From time to time, staff investigations may reveal conduct that warrants referral to professional licensing boards or similar organizations, such as a state bar association, accountancy board, professional association or self regulatory authority that performs a similar function.

Referrals for professional misconduct are considered Commission action. The Office of the Ethics Counsel in the General Counsel's Office has sub delegated authority to refer possible professional misconduct to professional licensing boards. Accordingly, the staff should follow the procedures described below when recommending that a professional be referred for possible misconduct. The decision to recommend that a professional be referred for possible misconduct should be made by officials at or above the level of Associate Director or Regional Head of Enforcement.

Attorney Misconduct:

- Contact the Ethics Office to discuss the situation.

- If the Ethics Office agrees to refer the attorney, the Ethics Office typically asks for more information, including the Action Memorandum and any public filings or if there are no existing documents, an email describing the attorney's conduct.

- The Ethics Office typically will forward all relevant public documents and an access request to the bar along with a referral letter describing the attorney's conduct. If there are no public documents, only the referral letter will be sent.

- The Ethics Office typically will periodically contact the State Bar to track the status of the referral.

Accountant Misconduct:

- If the Commission has decided not to take action against an accountant, but the staff believes the accountant's conduct warrants referral, staff should send its recommendation for referral to the Ethics Office, following the procedures for attorney referrals.

- If the Commission has taken action against a certified public accountant, the Office of the Chief Accountant ("OCA"), rather than the Ethics Office, will evaluate whether a referral is appropriate. Staff should notify OCA of any action against a CPA, even if his or her conduct did not relate to his or her position as an accountant. If

appropriate, OCA will notify the appropriate State Board of Accountancy of the action and forward the relevant public documents.

Considerations:

- Generally, a referral is appropriate when the staff recommends and brings an enforcement action against a professional. However, in some cases even when an enforcement action is not appropriate, the staff may believe the professional's conduct warrants referral. Assigned staff should discuss possible referrals with their supervisors.

- The Division typically does not refer matters to private bodies that perform functions analogous to government agencies. For example, informal referrals are not made to private bar associations, the American Institute of Certified Public Accountants, or the Association for Investment Management and Research.

- Though most referrals concern attorneys and accountants, the Ethics Office may also refer other professional misconduct to the appropriate licensing body.