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Trump's SEC Likely To Shrink Back Where White's Expanded

By **Carmen Germaine**

Law360, New York (November 16, 2016, 11:19 PM EST) -- U.S. Securities and Exchange Commission Chair Mary Jo White's signature policy of demanding admissions in cases of egregious fraud will likely remain when she steps down in January, but experts said her eventual replacement will probably pull back from her "broken windows" enforcement style and slow the agency's rulemaking flow.

White announced Monday that she will leave the agency when President Barack Obama leaves office, concluding a tenure marked by an aggressive enforcement policy and a significant expansion of the SEC's regulatory framework. According to former SEC enforcement officials and other experts, her departure could bring significant changes to the agency, which may face a shortfall in commissioners and will likely be helmed by a successor who brings a more cautious approach than the former federal prosecutor.

"Any change in the SEC chairmanship is bound to be disruptive, [but] I think the appointment of a new chair under the Trump administration is likely to have a seismic impact on the SEC," said Coates Lear, a principal at Squire Patton Boggs LLP and a former SEC enforcement attorney.

White, a former Debevoise & Plimpton LLP partner, became the agency's chair in April 2013. In her time as chair, the agency has brought a record number of enforcement actions, obtaining judgments worth more than \$13.4 billion. She also led the implementation of an array of new rules, many mandated by the Dodd-Frank Act, such as new safeguards in the security-based swaps market, and oversaw reforms to the money market fund industry and regulation of credit agencies.

But the agency could be set for significant change. President-elect Donald Trump has said he will dismantle Dodd-Frank and "replace it with new policies to encourage economic growth and job creation." He also pledged to institute a moratorium on all new regulations.

The SEC has already completed the bulk of its Dodd-Frank rulemaking, most of it under White's watch, but some rules remain on its to-do list, including those governing security-based swaps, executive compensation and asset-backed securities.

White told the House Financial Services Committee in written testimony for a Tuesday hearing that the agency will complete more Dodd-Frank rulemaking before she leaves, saying she expects to finalize the regulatory structure for security-based swap dealers by year's end.

But experts said White is unlikely to rush through other rulemaking in an effort to complete it.

Republican lawmakers have already cautioned White against scrambling to finish regulations before she leaves office. House Financial Services Committee Chairman Jeb Hensarling, R-Texas, told White in the Tuesday hearing that "midnight rulemaking" is "neither conducive to sound policy nor consistent with principles of democratic accountability."

Lori Echavarria, a partner at WilmerHale and former head of enforcement at the SEC's Los Angeles regional office, said White is even less likely to rush rulemaking because she is "a very practical,

prudent leader."

"I think it will be more business as usual," Echavarria said.

The situation will likely be much the same on the enforcement side, experts said.

"From an enforcement perspective, I wouldn't really expect any significant deviation from their current priorities during the remainder of her term," said Brad Mroski, a director at turnaround firm AlixPartners and former assistant chief accountant in the SEC's Division of Enforcement.

A Familiar Face

The bigger change, experts said, will come after White steps down. It's hard to guess who Trump might pick to replace her, but there's one significant clue: Trump has picked former SEC Commissioner Paul Atkins to recommend financial policies and related appointments, according to media reports.

Atkins, now the CEO of Patomak Global Partners LLC, served as a Republican commissioner from 2002 to 2008. As commissioner, he earned a reputation for opposing expansive regulation — he joined Commissioner Cynthia Glassman in dissenting from the commission's decision to adopt Regulation NMS, a package of major market reforms, saying it could have a detrimental impact on competition and innovation.

He's also spoken out against levying high penalties for corporate wrongdoing, saying high fines harm shareholders, and cautioned against using enforcement actions as a substitute for regulation.

"Discretion must not serve as a license to the SEC to test novel theories of liability and 'push the envelope' of the law," he said in a February 2008 speech.

Sen. Elizabeth Warren, D-Mass., has already spoken out against Atkins' role on Trump's transition team, saying in a letter to Trump that the former commissioner "aggressively opposed holding Wall Street accountable for defrauding investors."

With Atkins helming the search for a new chair, experts said, Trump is likely to select someone with a similarly narrow view of enforcement and regulation.

John F. Sylvia, co-chair of the securities litigation practice at Mintz Levin Cohn Ferris Glovsky and Popeo PC, said Atkins himself could become the nominee for chair, or he might put forward another former SEC commissioner, Daniel Gallagher, who also works with Atkins at Patomak. Gallagher has also earned a reputation for restraint, and has argued the Dodd-Frank Act "backfired" and "strangl[ed] our economy."

Putting on the Brakes

Whoever is selected, experts said, that person is unlikely to continue White's pace of rulemaking, especially when it comes to rules mandated by Dodd-Frank.

"A chair appointed by Mr. Trump would probably, at least temporarily, put the brakes on rulemaking pursuant to Dodd-Frank, given the president-elect's stated views on Dodd-Frank," Squire Patton's Lear said.

Other regulation opposed by Republican lawmakers could also be tabled, experts said. Congressional budgets have already included riders preventing the SEC from moving forward with plans to require companies to disclose political contributions, and talk of a uniform fiduciary rule for investment advisers and broker-dealers modeled on the U.S. Department of Labor's could also be put on the back burner.

More subtle changes could come to the SEC's enforcement program. Experts noted that the agency's current director of enforcement, Andrew Ceresney, is likely to leave with White. The pair have worked together for decades, collaborating at the Manhattan U.S. Attorney's Office and Debevoise before White brought Ceresney with her to the SEC.

White is known in part for her "broken windows" approach to policing the securities markets, calling on the SEC to be the "tough cop" on the beat by "pursuing all types of violations of our federal securities law, big and small."

Under a Trump-appointed chair and enforcement director, however, Sylvia said the agency may revisit the "broken windows" concept to evaluate whether it has actually made a difference.

Kathleen Marcus, co-chair of the enforcement defense and investigations practice at Stradling Yocca Carlson & Rauth PC and a former SEC enforcement attorney, noted that Republican administrations often pull back on enforcement.

"I would not anticipate that we're going to see a more robust program for enforcement under the Trump administration than we are seeing currently under the Obama administration and with Mary Jo White, as a former federal prosecutor, sitting as chair," Marcus said.

Other possible changes under a new chair could have an outsized impact as well. Lear said the agency could revisit policies like one that delegates authority to open investigations to Enforcement Division staff.

Under SEC rules, commission staff must obtain a formal order from the commission in order to open an investigation and subpoena witnesses. The commission originally issued such orders itself, but after the financial crisis, it delegated that authority to associate directors in the Enforcement Division to speed up the process.

"I think it's fair to say that that change has really emboldened the enforcement staff," Lear said. "I wouldn't be at all surprised if a new chair and a new enforcement director at least took a look at that policy."

If the commission does decide to take formal order authority away from staffers, Echavarria said, the change won't completely disrupt investigations — but it will noticeably slow them down.

"The commission will move quickly if they need to in approving formal orders authority, but in general, the approval process will go from a day or a week to get a formal order to probably a couple of weeks or longer," she said.

The SEC could also decrease its use of its administrative courts, which have attracted criticism from respondents who feel the court lacks the due process protections of an Article III court and argue the agency's judges are biased.

The SEC uses its administrative court partly because cases filed in-house take less time to litigate, and Marcus said a switch to federal courts could slow things down while giving defendants more due process rights.

"If they decide to pull back on enforcement, that is a lever they could push," Marcus said.

Sylvia agreed that a new chair will likely move more cases to federal court, but he said that trend has already started in the last year under White. He said the move appears to be partly in response to the criticisms the agency has fielded, but also a reaction to limited administrative court resources.

"There are only so many SEC administrative law judges to handle these cases," Sylvia said.

A Scaled-Back Admissions Policy

Amid the changes, experts agreed one policy of White's is likely to survive the transition: her admissions policy.

Under that policy, the agency requires companies and individuals to admit wrongdoing in cases of egregious fraud as part of an effort to increase accountability.

Lear said that change is likely to be White's biggest legacy.

"That was a dramatic sea change in the way that the commission approached settlements," Lear said. "Obviously, the vast majority of cases continue to be settled on a no-admit-no-deny basis, but the possibility that the commission might insist upon admissions in a settlement looms in the background of every case."

But the policy has come under fire for its lack of transparency, and admissions have only been sought in a handful of cases since White announced the change.

Because the policy is still rarely used, Sylvia said, future chairs will probably keep it around as a tool, even if they use it even less than White's agency has.

As the agency considers when to seek admissions, Echavarria noted the calculus for the new chair might also differ as the commission carefully considers how to apply the policy to corporate entities and avoid "overcriminaliz[ing]" the SEC's practice.

"I think there will be more interest in having the commissioners themselves involved in making decisions about whether there will be admissions or not," Echavarria added.

A Commissioner Shortage

Before a new chair ever enters the SEC offices, however, experts said the agency could face a significant hurdle if White steps down before her replacement is nominated, as it may be forced to function with only two commissioners.

The SEC has been short on commissioners for a year, functioning with only White, Republican Commissioner Michael Piowar and Democratic Commissioner Kara Stein.

President Obama nominated Republican Hester M. Peirce, a senior research fellow at George Mason University's Mercatus Center, and Democrat Lisa M. Fairfax, a George Washington University School of Law professor, in October 2015 to fill the spots left by Democrat Luis Aguilar and Republican Daniel Gallagher. But their nominations have been languishing in the Senate.

Echavarria noted that Peirce is closely tied with Atkins. She served as his counsel while he was a commissioner and has been a vocal critic of the Dodd-Frank Act, even writing a book titled "Dodd-Frank: What It Does And Why It's Flawed," making it more likely Trump will continue with her nomination.

"I think she would be someone who would make sense for the Trump administration to continue to support as a nominee," Echavarria said.

If Trump decides not to move forward with Fairfax, he'll have to select another Democratic nominee. Even if he doesn't withdraw either nomination, delays in the Senate could mean only Piowar and Stein are left on the commission when White steps down in January.

In that case, Marcus said, it's likely Piowar will be anointed as interim chair until a new chair is nominated.

The agency will still be able to function, Marcus said, since under revised agency rules, the commission can have a quorum with just two commissioners — though they will only be able to move forward on issues and cases they agree on.

"With a Democrat and a Republican remaining, you could have loggerheads," Marcus said.

In the end, whatever happens in White's absence, the agency is poised for significant change. Lear noted that the transition will involve a tremendous amount of staff movement, especially at the top of the agency.

"I think in a Trump administration, there are likely to be a lot of new faces," he said.

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