

**Legal Risk Management Tip**  
**December 2013**

**2013 SEC ENFORCEMENT CASES – A YEAR IN REVIEW**

As part of its “Fiscal Year 2013 Agency Financial Report” released by the Securities and Exchange Commission (“SEC”) on December 17, 2013, the SEC discussed how the agency’s new and “more aggressive enforcement actions” fared in 2013. According to the report, the SEC ended the fiscal year of 2013 with 686 enforcement actions, including 402 in the last six months of the year. Furthermore, the SEC stated the resulting disgorgement and monetary penalties arising from these enforcement actions totaled \$3.4 billion - representing a ten percent (10%) increase from 2012, and a twenty-two percent (22%) increase from what was seen in 2011. The SEC noted that the “outstanding quality” of the enforcement actions was a major factor in the rising monetary penalties figure. Below is a summary of some of the more notable cases seen in 2013.

**Insider Trading**

*Securities and Exchange Commission v. CR Intrinsic Investors, LLC et al.*, Civil Action No. 8466 (VM). Hedge fund advisory firm CR Intrinsic Investors LLC, an affiliate of S.A.C. Capital, agreed to the largest insider trading settlement in SEC history, settling charges that it participated in an insider trading scheme involving a clinical trial for an Alzheimer’s drug. According to the SEC, in 2008 two S.A.C. portfolio managers obtained material non-public information (“MNPI”) about three publicly traded companies. The portfolio managers admitted to the firm’s owner, Mr. Cohen, that they may have obtained MNPI to support their trading. Even with this knowledge, Mr. Cohen failed to take reasonable steps to investigate and prevent securities law violations and permitted the trade executions. Under the terms of this historic settlement, CR Intrinsic was required to pay more than \$600 million, including disgorgement of nearly \$275 million, \$52 million in prejudgment interest and a \$275 million penalty.

**False Statement and Failure to Supervise**

*In the Matter of JP Morgan Chase & Co.*, IA Rel No. 70458 (Sep. 19, 2013). The SEC charged J.P. Morgan Chase & Co. with misstatements of its financial results and a lack of effective controls to prevent or detect a scheme to conceal the extent of massive trading losses. The SEC previously charged two former JPMorgan traders with committing fraud to hide the massive losses in one of the trading portfolios in the firm’s Chief Investment Office (“CIO”). The SEC’s subsequent action against JPMorgan faults its internal controls for failing to ensure that the traders were properly valuing the portfolio, and its senior management for failing to inform the firm’s audit committee about the severe breakdowns in the CIO’s internal controls.<sup>1</sup> J.P. Morgan settled the charges, admitting publicly that it had violated Federal securities laws and paying a \$200 million penalty.

**Failure to Report Personal Trades**

*In the Matter of Carl D. Johns*, IA Rel No. 3655 (Aug. 27, 2013). The SEC sanctioned former portfolio manager Carl Johns (“Mr. Johns”) of Boulder Investment Advisers (“BIA”), a

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<sup>1</sup> See, <http://www.sec.gov/news/digest/2013/dig091913.htm>

Colorado-based investment adviser, for forging documents and misleading the firm's Chief Compliance Officer ("CCO") (who was not named in the SEC's Release) in order to conceal his failure to report personal trades, in violation of Rule 38a-1(c) of the Investment Company Act of 1940 (the "'40 Act"). This violation was discovered by the CCO herself, thanks to BIA's well-drafted policies and procedures ("P&Ps") and the CCO's supervisory efforts and administration of those P&Ps. The SEC alleged that Mr. Johns failed to pre-clear several hundred securities trades in his personal accounts, as is required under Rule 17j-1 of the '40 Act, and as specified in BIA's Code of Ethics. Mr. Johns even went so far as to create false documents purporting pre-trade approvals, in an attempt to mislead the CCO in her investigation into Mr. John's improper trading. The CCO's efforts eventually lead to the discovery of Mr. Johns' improprieties, at which point BIA self-reported the case to the SEC. Mr. Johns settled the charges with the SEC, agreeing to pay disgorgement of \$231,169, prejudgment interest of \$23,889, and a penalty of \$100,000. Additionally, Mr. Johns consented to a five (5) year bar from the industry.

### **Failure to Register**

*In re: Ranieri Partners LLC et al*, SEC Administrative Proceeding, No. 3-15234; and *In re: Stephens*, SEC Administrative Proceeding, No. 3-15233. In this case, Ranieri Partners LLC allegedly hired a third-party, Mr. William Stephens, to find investors for a private fund. According to the SEC, Stephens offered strategy analyses and key documentation to prospective clients, going far beyond what should have been his limited role in acting as a "finder" responsible for making initial introductions. For these actions, Stephens should have had to register as a broker-dealer before performing any such activities. The SEC also brought actions against Donald Phillips, a Ranieri senior managing director at the time, for allegedly aiding the violations by providing materials to Stephens and ignoring "red flags" about Stephen's improper conduct. For his part, Phillips agreed to pay a \$75,000 penalty. Stephens was ordered to repay \$2.42 million plus \$410,000 in interest he earned for his efforts on behalf of Ranieri, which was ultimately waived by the SEC due to Stephen's financial condition. Stephens was permanently barred from the securities industry.

### **Conclusion**

The SEC is increasing its examination focus in 2014 and utilizing new methods - such as new task forces and technology improvements to improve technical and analytical capabilities. The SEC also has reported that it has a very strong "pipeline" already developed for next year in that it has opened 908 investigations and obtained 573 formal orders of investigation. With this in mind, firms should take time at the end of this year to review the adequacy of its internal controls in these, and other areas, to help mitigate potential risks going into 2014.

For more information, please contact Jacko Law Group, PC at (619) 298-2880 or email us at [info@jackolg.com](mailto:info@jackolg.com). Have a very happy holiday season.

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