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How Should You Respond When SEC Examiners Come Knocking?

PHOENIX – How a dealer or municipal advisor responds to a Securities and Exchange Commission examination or enforcement investigation is crucial in determining the outcome, lawyers and an SEC official said Thursday.

The comments were made during a pair of panels focused on topics and trends in securities law and SEC enforcement during the first day of the National Association of Bond Lawyers' Tax and Securities Law Institute. Panelists spoke about the process and pitfalls of both examinations by the SEC's Office of Compliance Inspections and Examinations (OCIE) and investigations by the commission's Enforcement Division's Public Finance Abuse Unit.

Nadine Sophia Evans, an OCIE attorney, said that the SEC has seen a lot of registration failures among municipal advisors, who are required to be registered with both the SEC and with the Municipal Securities Rulemaking Board if they provide muni bond-related advice to municipal issuers and other entities. Also frequent among MAs are books and records deficiencies and supervisory system shortcomings, Evans said. OCIE's current MA exam priority is independent MAs that who are not dual-registered as broker-dealers, she said.

When the SEC has seen failures with respect to the fiduciary duty — a duty created for MAs by the Dodd-Frank Act requiring them to put the interests of their municipal issuer clients ahead of their own — Evans said it has typically been related to a failure to disclose a conflict of interest such as a competing business arrangement. Whether a problem is handled by OCIE, the enforcement staff, or the Financial Industry Regulatory Authority, depends on a variety of factors, Evans said.

But several panelists agreed that how the target of an SEC exam or investigation reacts is crucial.

Evans said that OCIE offers registrants a chance to have an "open conversation" with the SEC about the preliminary findings, and that findings of deficiency are kept confidential inside the SEC. But a lawyer at the session said that litigation experience has taught her that there's "no such thing as an 'open conversation' with anyone from the SEC."

Nadine said that litigation is a different matter from a less formal discussion with OCIE. Andrew Kintzinger, a panelist who practices with Hunton & Williams in Washington D.C., cautioned that statements freely given to OCIE can bite firms later because they can be used against the firms by the Enforcement Division.

"The legal concern is still there," Kintzinger said. "Voluntary today can be treated as an admission tomorrow."

In a later panel Kathleen Marcus of Straddling Yocca Carlson & Rauth in Newport Beach, Calif., warned against taking a hostile view of SEC attorneys. SEC lawyers view themselves as regulators rather than as the enemies of the firms they are looking into, she said, and being professional them is best.

“Being very adversarial … it’s not going to end well,” she said. Enforcement actions could even be avoided with cooperation in some cases, panelists said.

The OCIE said in its recently-published priorities that it is also going to be focusing on examining the MSRB.

Michael Post, general counsel of the MSRB who was also a panelist, said that the board was recently examined with respect to its compliance with federal regulations aimed at safeguarding the technological infrastructure of the market. The MSRB has faced larger OCIE exams before and is apparently due for another, Post said.

“We produce thousands of documents to OCIE in those processes,” Post said, adding that he believes the MSRB’s experience is probably not unlike the experience of a registered entity like a dealer.

Panelists also discussed takeaways from recent SEC enforcement actions, noting that they have generally contained an element of public corruption such as when the commission in November charged Oyster Bay, N.Y. with hiding the existence and potential impact of side deals with a businessman who owned and operated restaurants and concession stands.

Evans said that the SEC is going to continue focusing on disclosure. “I don’t think that theme is going away anytime soon,” she said.

The NABL conference concludes Friday afternoon.

By Kyle Glazier

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