



January 14, 2010

## SEC Issues Important New Guidelines on Cooperation

As promised by Enforcement Director Robert Khuzami, the U.S. Securities and Exchange Commission (SEC) has announced the most important changes to its cooperation program since articulating a framework for evaluating cooperation by companies in the Commission's 2001 *Seaboard* Report. On January 13, the Commission for the first time issued a Policy Statement describing how it will evaluate cooperation by individuals. (*Available at <http://www.sec.gov/rules/policy/2010/34-61340.pdf>*.) In addition, the Enforcement Staff announced that it would be using several cooperation tools that have been utilized by criminal authorities in recent years with great success.

Calling the new measures "a potential game-changer for the Division of Enforcement," Director Khuzami said in a press release that "[t]here is no substitute for the insiders' view into fraud and misconduct that only cooperating witnesses can provide." (*See <http://www.sec.gov/news/press/2010/2010-6.htm>*.) With respect to individuals, the Commission announced that it would evaluate four considerations in deciding whether and how to credit an individual's cooperation:

For more information, contact:

**Russell G. Ryan**  
(202) 661-7984  
rryan@kslaw.com

**Matthew H. Baughman**  
(404) 572-4751  
mbaughman@kslaw.com

**King & Spalding**  
**Washington, DC**  
1700 Pennsylvania Avenue, NW  
Washington, DC 20006-4706  
Tel: (202) 737-0500  
Fax: (202) 626-3737

**Atlanta**  
1180 Peachtree Street, NE  
Atlanta, Georgia 30309-3521  
Tel: (404) 572-4600  
Fax: (404) 572-5100

[www.kslaw.com](http://www.kslaw.com)

- The assistance provided by the individual, including the timeliness of the individual's cooperation, the quality of the cooperation, whether it was voluntary or required by the terms of another agreement with a law enforcement or regulatory organization, and whether the individual encouraged or authorized others to assist the Staff;
- The character and importance of the underlying matter, including whether the subject matter is a Commission priority or involves serious, ongoing, or widespread violations of the securities laws presenting harm to investors;
- The interest in holding the individual accountable, including the severity of the misconduct, the culpability of the individual, whether the individual tolerated or took steps to prevent the illegal activity, and the efforts taken to remediate any harm caused by violations; and



## Special Matters & Government Investigations Practice Group

- The profile of the individual, including the history of lawfulness, acceptance of responsibility, and whether the individual is licensed, associated with a regulated entity, has fiduciary responsibilities regarding financial matters, or is an officer, director, or member of senior management of a public company.

The Enforcement Division also authorized its Staff to use three cooperation tools that are quite familiar to criminal prosecutors – cooperation agreements, deferred prosecution agreements, and non-prosecution agreements. Although the Staff in the past may have decided not to recommend enforcement action against an individual or company based on cooperation, these new agreements will be written documents explicitly memorializing what action the SEC or its Staff will agree to take (or decline to take) in exchange for an individual’s or company’s cooperation and agreement to comply with particular undertakings. In addition, the Commission delegated to the Enforcement Director the authority to submit witness immunity requests to the Department of Justice, requesting that an individual’s statements not be used against the individual in a criminal case.

In discussing the anticipated guidelines on December 8, 2009, Director Khuzami pointed out that the new cooperation regime “will have other consequences, such as in the area of representation of multiple witnesses by a single lawyer or law firm . . . . [T]he broader availability of cooperation credit will increase the risk of conflicts of interest in situations where counsel seeks to represent multiple clients. It may be in the interest of one client to be the first to report the misconduct to the Commission or offer his or her cooperation. But, obviously, only one client can be first.” Khuzami’s comments highlight that while the new rules will present potentially beneficial opportunities for individuals and companies seeking credit for cooperation, they also pose difficult challenges ahead for both would-be cooperators and the lawyers who will represent them.

Two such challenges are immediately apparent. First, according to the Policy Statement, cooperation agreements will be entered into between the cooperating party and the Division of Enforcement only—*i.e.*, they will not be binding on the Commission itself, which will retain discretion to reject the Enforcement Staff’s judgment and disregard an agreement in the ultimate charging decision. Thus, even with a signed cooperation agreement in place, the cooperator remains at some risk that the agreement will not be honored by the Commission, although we hope and expect such cases will be exceptionally rare. Deferred and non-prosecution agreements, by contrast, will require a Commission decision to forego enforcement action against the cooperator in exchange for cooperation and compliance with express prohibitions and undertakings.

A second challenge involves interpreting the factors listed by the SEC as relevant in determining whether and how much to reward cooperation by individuals. While most of the factors are straightforward, some are not entirely clear in terms of what the SEC will consider favorably versus unfavorably (e.g., those referring to the “character” and “importance” of the matter under investigation, the extent of the harm from the violation, how old the violation is, etc.). One fair reading would be that rewards will be greater for cooperation in investigations where the overall misconduct was most egregious and most recent, but only if and to the extent that the cooperator’s own culpability is relatively low. However, that interpretation is far



## Special Matters & Government Investigations Practice Group

from obvious, and it may take months or years of experience with the Policy Statement, or additional guidance, before a confident assessment of the Commission's intent can be made.

Please contact us if you have any questions regarding these developments or any other SEC enforcement issues.

*King & Spalding is an international law firm with more than 800 lawyers in Abu Dhabi, Atlanta, Austin, Charlotte, Dubai, Frankfurt, Houston, London, New York, Paris, Riyadh (affiliated office), San Francisco, Silicon Valley and Washington, D.C. The firm represents half of the Fortune 100 and, according to a Corporate Counsel survey in August 2009, ranks fifth in its total number of representations of those companies. For additional information, visit [www.kslaw.com](http://www.kslaw.com).*

*This alert provides a general summary of recent legal developments. It is not intended to be and should not be relied upon as legal advice.*