



At the Practising Law Institute's annual SEC Speaks conference, U.S. Securities and Exchange Commission (SEC) leadership highlighted the agency's current enforcement priorities and previewed its agenda for the year to come.

The in-person conference, held in Washington, D.C., on September 8-9, 2022, covered wide-ranging topics, including the SEC's successful enforcement actions; proposed environmental, social, and governance (ESG) regulations; and market implications of the Russia-Ukraine conflict. In various panel discussions dominated by rapidly evolving market conditions, though, the agency exhibited a laser-like focus on its regulation of cryptocurrency, which is still developing.

The tone was set from the start with SEC Chairman Gary Gensler quoting Justice Thurgood Marshall in admonishing that "Congress painted the definition of a security with a broad brush." Under this expansive

framework, Gensler and the SEC leadership laid out the agency's plans to adapt existing regulations and judicial precedent to address market innovations and police emerging sources of risk.

Below are five key takeaways emerging from this year's conference:

## 1. "Main Street" Goes Digital: The SEC Pushes Crypto Assets to the Forefront

Chairman Gensler used his [opening remarks](#) to send an unequivocal message that the SEC's "investor protection" mission extends to the cryptocurrency market. Quoting inaugural SEC Chairman Joseph Kennedy (*circa* 1935), Gensler emphasized that "no honest business need fear the SEC" and declared that nothing about the crypto market is incompatible with the reach of current securities laws. Chairman Gensler asserted that the "vast majority" of the nearly 10,000 crypto tokens in existence are securities that fall within the ambit of the federal securities regulations. He added that where crypto "intermediaries" function as exchanges, brokers, or dealers—e.g., matching orders of buyers and sellers, effecting transactions, or acting in a custodial capacity—they should assess their registration obligations. The chairman further encouraged intermediaries to register each of their independent functions, which in some cases could result in disaggregating into separate legal entities to mitigate potential conflicts of interest and bolster investor protection.

Other SEC leaders also emphasized the commission's focus on crypto. For example, staff from the Office of the Chief Accountant (OCA) observed that entities safeguarding crypto assets on behalf of other parties do not always "transparently" disclose to their own investors the unique technological, legal, and regulatory risks they face. Staff from the Office of International Affairs (OIA) flagged as key concerns "unbacked" crypto, stablecoins, and decentralized finance (DeFi) trading platforms. Staff from the Enforcement Division's Market Abuse Unit (MAU) signaled that they ignore financial product "labels" and view many crypto cases as relatively straightforward under current securities laws.

## 2. Enforcement Maintains Focus on Individual Accountability

In his [remarks](#), Division of Enforcement Director Gurbir Grewal explained that in bringing enforcement actions, the SEC not only seeks to impose accountability and incentivize compliance but also aims to bolster investor trust and confidence. Included in this "regulation-by-enforcement" agenda are individuals who play gatekeeper roles within regulated entities.

Expanding on Director Grewal's comments, Division of Enforcement Chief Counsel Samuel Waldon focused his remarks on three mechanisms through which the SEC seeks to impose individual liability:

- **Section 304 of the Sarbanes-Oxley Act.** In short, [SOX 304](#) provides that if an issuer is required to prepare an accounting restatement "as a result of misconduct," then the CEO and CFO must reimburse the company for "any" bonus, incentive, or equity-based compensation received in the prior year and any profits realized from selling the company's stock in the prior year. In deploying this provision, Chief Counsel Waldon emphasized that the statute "applies to culpable and *nonculpable* CEOs and CFOs, alike" and that the SEC can bring an action seeking *all* compensation subject to SOX 304—not just the amount by which an officer's compensation was inflated because of the misconduct at issue.
- **Director and officer bars.** Chief Counsel Waldon described D&O bars as a "powerful" remedy that the Enforcement Division will seek "more broadly." In addition to the usual circumstances under which such bars are sought, Waldon stated that the division will also seek bars in the form of "equitable" judicial relief, including sanctions based on an individual's character and fitness. Waldon even suggested D&O bars as a prophylactic measure in cases where the defendant has not previously served as an officer or director but could do so in the future.
- **Disgorgement litigation after *Liu v. SEC*.** Finally, the U.S. Supreme Court's decision in [Liu v. SEC](#) affirmed the SEC's authority to seek disgorgement but limited such amounts to the wrongdoer's net profits

and allowed legitimate expenses to be deducted from that total. In his remarks, Waldon underscored that it remains the defendant's obligation to adequately support any expenses that are being claimed as a deduction cited to reduce disgorgement. Expounding upon a question left unanswered after *Liu*, Waldon stated that the SEC will continue seeking disgorgement in cases where it is not feasible to return disgorged funds to investors. Instead, the monies are deposited with the U.S. Department of the Treasury (a practice the Court questioned but did not specifically address in the *Liu* decision).

### **3. Cybersecurity Disclosures: A Continued SEC Priority**

The SEC staff highlighted that cybersecurity disclosures continue to be an area of focus and explained that several studies demonstrate that cybersecurity risk is a top investor concern. A March 2022 [proposed rule](#) aims to provide investors with more timely and consistent disclosures to address these concerns. Notably, the proposed rule requires registrants to report material cyber incidents on Form 8-K, meaning such events would need to be disclosed within four business days after the registrant determines that it has experienced a material incident. As proposed, the rule would also amend Form 10-K to require periodic disclosures regarding policies and procedures that aid registrants in identifying and managing cyber risks and management's role in implementing those policies and procedures.

David Hirsch, chief of the Enforcement Division's Crypto Assets and Cyber Unit, emphasized the importance of reporting cyber breaches and added that after a breach, issuers should be on heightened alert for indicia of insider trading and focus on protecting any personally identifiable information (PII) or other sensitive information that may have been compromised.

### **4. The SEC Sheds Light on ESG Enforcement**

Last year's launch of the SEC's Climate and ESG Task Force within the Division of Enforcement cemented the agency's emphasis on ESG and climate-related issues, but we continue to see how enforcement in this space may develop. Enforcement staff highlighted a recent action brought against an investment advisor based on alleged misrepresentations that its fund investments had undergone an ESG quality review. Enforcement staff emphasized that a "good lesson" for advisors who recommend ESG-related strategies is to also ensure that disclosures comport with ESG rules and regulations.

Moreover, Enforcement staff noted that the Asset Management Unit in particular will be focused on ESG and climate-related disclosures to determine whether they contain accurate representations. Division of Examination personnel expressed their focus on whether advisors are providing "accurate and adequate disclosures" on Form CRS items, including those related to climate risks, and on how well entities have remediated previously identified deficiencies. These comments come on the heels of the SEC's recent [proposed rules](#) to enhance ESG disclosures for investment advisors and investment companies. Given the extended commentary about ESG, it would not be surprising if enforcement actions continued to ramp up in the coming year.

### **5. A New Focus on Emerging Risk Disclosures, Including the Russia-Ukraine War**

Finally, the SEC will focus on ensuring registrants make adequate disclosures in areas of emerging risk in the upcoming fiscal year, including risks associated with the Russia-Ukraine war, supply chain issues, and inflation. Echoing a theme imbuing many of the SEC Speaks presentations where staff cited the Russia-Ukraine conflict as a serious challenge to businesses, Division of Corporate Finance staff advised that registrants should consider the need for disclosures regarding the Russia-Ukraine war even if registrants do not conduct business in those countries. This conflict could exacerbate supply chain disruption, which was borne out of the pandemic and contributed to inflationary pressures, causing constraints on businesses and the economy. More broadly, inflation has led to the increased cost and decreased demand for products and services. The staff advised registrants to consider whether these developments affect their business and, if so, to avoid boilerplate in their

communications and disclosures. The Division of Corporate Finance also [announced](#) plans to add units within its Disclosure Review Program to evaluate disclosures in issuer filings involving crypto assets and certain life science companies.

## Takeaways

Throughout the conference, SEC staff emphasized new areas of importance, such as cryptocurrency and ESG disclosures, and highlighted continued areas of focus, such as cybersecurity and individual accountability. For now, it appears SEC leadership is taking somewhat of a "one size fits all" approach to regulating these various issues—working within the existing securities law framework and tackling any nuances through other means, such as rulemaking, enforcement actions, and settlements. The regulation-by-enforcement environment means that issuers and regulated entities would be well served by dedicating compliance resources to the SEC's enforcement priorities and staying attuned to the developing legal landscape.

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