

# The US (SEC) regulatory reaction in light of the financial crisis: What does this mean for Europe?

Patrick J. O'Malley, Esq.  
Bocconi University  
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# The Crisis

- By “crisis”, referring to the sub prime credit crisis beginning in earnest in summer/fall 2007 onwards, of course brunt of it hit a year ago
- Here, focus on SEC (Securities and Exchange Commission) actions in relation to capital markets & corporate governance in light of corporate scandal relating to/leading to the downturn
- Great public outcry ( especially by popular and financial press), esp. Sept. 2008 onward

- Heavy blame fell on SEC , and other (banking) authorities, for contributing to the Crisis, inter alia,
  - Lack of proper transparency & corporate disclosure in relation to certain types of financial instruments, & overall regarding trading / risk analysis (e.g. AIG w it's immense exposure to subprime mortgage default swaps- \$180B)
  - Massive financial institution indebtedness & related risk-taking (i.e. Net Asset Rule exemption in 2004)
  - Failure to wise up to frauds of Bernie Madoff & others (ultimately failed to follow up, investigate well\*)
  - For ex. Madoff 's \$50 B scam went on for yrs: but 3 examinations & 2 investigations 92-08

# More problem points

- Executive pay packages full of perverse incentives, rewarding short-term greed and even failure, taking on enormous also the risk
- Lack of properly regulating certain established “grey area” practices (short selling of shares, dark pools, flash orders)
- Failure to properly regulate the whole rating industry / the agencies

- Popular outcry/blame is not new- look at wave of corp scandals shaking US earlier this decade: ENRON, Tyco, WorldCom Etc etc.- a *“Gatekeeper” that has repeatedly dropped the ball*
- Paradoxically, SEC has been the most active, & feared, corporate/market regulator in the world, when compared to int’l counterparts: but Sept. 2008 humiliated them

# Positives: Why feared?

- Extensive enforcement actions against:
    - Insider trading at all levels
    - Misleading &/or false corp disclosure (e.g. \$50 fine imposed on Gen. Electric in Aug.-over \$1 B improperly recognized over 5 yrs)
    - Market manipulation and abuse
    - The stock option dating scandal ( West Coast/high-tech focused)
    - With DOJ, corporate corruption through the FCPA ( Foreign Corrupt Practices Act)
    - All manner of investment scams
- Thus, the SEC offers an uncomfortable paradox.

# US regulatory response to the crisis

- To date, extensive short-term & long-term actions taken against both symptoms & causes of crisis by a host of US regulatory agencies (often in coordination w European & global counterparts)
- Far too complicated, wide-ranging to cover here
- Situation is fluid and in great flux, could change direction (even dramatically) due to both economic and political developments
- Not clear exactly what the “final rules” for corporations and financial situations will look like- lots of proposals by Obama/Treasury, Congress, regulators/SEC themselves, also international level initiatives (G-20)
- Ergo we are looking at a rapidly-changing “snapshot” here

# Obama's road map for increased regulation (June 2009)

- Hedge funds & other private pools of capital would have to register w SEC
- 1000s of financial institutions would be required to increase capital reserves to protect against unexpected losses, & cos would also have to keep part of credit risk for loans they have packaged into securities
- State would have powers to take over & unwind large financial cos, power gov't did not have last year when the financial crisis was exploding
- Federal Reserve would be granted more powers over payments & settlements systems in US financial markets to prevent breakdowns officials fear could destabilize economy.



- Any large, interconnected company that the government wants to take over & break up could be seized by Treasury Dept., if certain conditions met
- Plan clearly grants central bank unprecedented new powers to conduct comprehensive examinations of almost any US financial company, as well as any of that company's foreign affiliates
- However, plans will inevitably change when it goes to Congress- also lots of legal/political challenges (some may well be unconstitutional, giving too much power to Feds over States & private businesses/individuals)

- In 14 Sept. 09 major address in NYC, Obama reiterated many of above points, repeating a call for a new Consumer Financial Protection Agency, an oversight council of regulators and stiffer capital & liquidity requirements for banks

# How might this affect EU firms, investors and regulators?

- Large EU publicly-listed companies having dual listings = direct application of most US securities & corporate governance laws
- EU companies privately placing shares with US institutional investors (QIBs) or private equity funds (e.g. 144A offerings)
- EU companies setting up US subsidiaries or a JV with a US counterparty (esp financial or insurance cos)
- Sometimes even purely EU tender offers/mergers (if US SHs, business or subs involved)

# How might this affect EU firms, investors and regulators?

- Any jurisdictional connections w US (e.g. Corrupt practices/payments)
- SEC & other US regs often influence national & EU regulators in their approaches to same problems, either in direct coordinate w US, or indirectly (in either case, “regulatory convergence”)
- Finally, business practices & expectations change- if regulations change in US, inevitably spread to European corp/capital market deals, esp. via the large investment banks

# The Players: The US SEC

- Mission is to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation
- NB a host of other federal and state agencies regulate the banking and financial/investment industries, as well as corporate capital raising activities, & have contributed (and will continue to do so) to the changing US regulatory landscape

# What is the SEC?

“There is hereby established a Securities and Exchange Commission ... to be composed of five Commissioners to be appointed by the President by and with the advice and consent of the Senate.” **Section 4(a)- Exchange Act of 1934**

- Created in 1934; HQ in Washington, D.C
- 5 Commissioners appointed by President, under the oversight of the US Congress – non-political in nature
- Staff of approx. 3500; c. 1/3 are qualified lawyers
- Primary mission – to protect investors and maintain the integrity of the securities markets
- Does this by maintaining & regulating the required accounting & disclosure rules firms must follow

# SEC responsibilities

- interpret federal securities laws;
- issue new rules and amend existing rules governing the US capital markets & the raising of capital;
- oversee the inspection of securities firms, brokers, investment advisers, and ratings agencies;
- oversee private regulatory organizations in the securities, accounting, and auditing fields; and
- coordinate US securities regulation with federal, state, and foreign authorities.

- The SEC oversees more than 30,000 registrants including 12,000 public companies, 4,600 mutual funds, 11,300 investment advisers, 600 transfer agencies, and 5,500 broker dealers.
- Approximately 1,150 of the 12,000 companies registered with the SEC are non-US companies (include a very large percentage of Europe's largest companies)
- NYSE: 424 companies from 45 jurisdictions at 20 December 2007
- NASDAQ: 303 companies from 35 jurisdictions at 12 August 2008



# The Commodity Futures Trading Commission (CFTC)

- Independent agency of US federal gov't
- Commodity Exchange Act prohibits fraudulent conduct in trading futures contracts: in 1974, Congress amended Act to create more comprehensive regulatory framework for trading futures contracts & created CFTC
- Mission is to protect market users & public from fraud, manipulation, & abusive practices related to sale of commodity & financial futures & options, & to foster open, competitive, and financially sound futures & option markets
- Trading in futures contracts has expanded rapidly beyond traditional physical & agricultural commodities into vast array of financial instruments, e.g. foreign currencies, US & foreign state securities, & US & foreign stock indices

# CFTC cont'd

- Aim to assure economic utility of futures markets by encouraging competitiveness & efficiency, ensuring integrity, protecting participants against manipulation, abusive trading practices, & fraud, & ensuring financial integrity of clearing process— allowing futures markets to serve important function of providing means for price discovery & offsetting price risk
- Numerous efforts by SEC to usurp its regulatory jurisdiction
- Obama's effort to reorganize regulation of entities such as hedge funds & products such as derivative contracts will provide SEC officials w another opportunity to attempt to expand SEC jurisdiction at expense of CFTC
- In fact, harmonization of enforcement programs of SEC & CFTC regulation is currently being implemented (although there are a number of practical problems, such as definition of 'insider trading' etc.)

## Other notable regulators: the US Dept. of the Treasury

- Mission: strengthen nat'l security by managing US government finances effectively, promoting economic growth & stability, & ensuring the safety, soundness, & security of US & int'l financial systems- key role as steward of US economic & financial systems
- Executive agency responsible for promoting US economic prosperity & ensuring financial security - responsible for advising President on economic & financial issues, encouraging sustainable growth, & fostering improved governance in financial institutions
- Works w other federal agencies, foreign states, & int'l financial institutions to encourage global economic growth, raise standards of living, & if possible, predict & prevent economic & financial crises
- Also performs critical/extensive role in enhancing national security by implementing economic sanctions against foreign threats, identifying & targeting financial support networks of national security threats, & improving safeguards of US financial systems

# Brief Overview banking regulation

- Office of the Comptroller of the Currency (Comptroller): charters and regulates federal/national banks
- The Federal Reserve system (Federal Reserve Board is the governing body): serves as US' central bank; FRB regulates state banks becoming FRS members (most are state-chartered, but part of a 'dual banking system')
- FSB regulates all bank holding companies (which US investment banks became)
- Various state banking regulators

# Brief Overview banking regulation

- The Federal Deposit Insurance Corporation (FDIC): has 2 roles- provides deposit insurance to all national banks & in its discretion to state banks; it regulates state banks purchasing its insurance but are not FRS members (NB temporary increase in deposit insurance from \$100,000 to \$250,000 per depositor through 31 Dec. 31 09)
- *Results in a regime of confusing and overlapping regulatory jurisdiction, considered by many to be inefficient*
- We will not deal with these developments here- focus on the capital markets and corporate governance

# Key principles of US securities laws (SEC of course has central role)

- Protect investors (esp. small ones), by requiring they get all material info to make good investment decisions = defense of trust in US capital markets (trust = wide shareholder base)
- Transparency at all times: bf purchase of shares, as a Shareholder, & at time of sale
- How? – regulations requiring complete, accurate, timely & not misleading disclosure

# Key principles of US securities laws & Corporate Governance (SEC focus)

- Honesty & frankness with Investors and the markets
- Insiders and institutionals can't profit at the expense of small investors/individuals
- SEC actively enforces its rules, against companies, individuals, funds, brokers, etc. for insider trading & other violations (sometimes w DOJ)

## Why securities/corp governance laws needed?

- Failure of the “Gatekeepers” to do their jobs & effectively / efficiently protect the integrity of the system
  - To wit, the first, second, third and fourth lines of defense of market trust (internal corporate persons-insiders, advisers, market participants & authorities)
- Repeated failures to ask questions:
  - Auditors, lawyers, banks, research analysts, press, SEC & other regulators



## Effects of failure, as seem with crisis and post-Enron

- Massive blow to the economy: access to capital and financing for consumers and businesses = reduced demand, productivity and job losses
- People suffer: especially small investors-- families
- “Investment portfolio” = US retirement savings, college fund
- TRUST is lost – destroys the fabric of our markets, confidence in investing

# US securities laws

- Both federal & state laws regulate securities
- Bf 1929 companies could issue stock at will
- Bogus corporations sold worthless stock; other companies issued & sold large amounts of stock w/o considering effect of unlimited issues on SHs' interests, value of the stock, & ultimately the US economy
- Federal securities law consists of a handful of laws passed between 1933 and 1940, as well as later laws. Federal laws stem from Congress's power to regulate interstate commerce

## Key US securities / corporate governance laws include:

- Securities Act of 1933
- Securities Exchange Act of 1934
- Trust Indenture Act of 1939
- Investment Company Act of 1940
- Investment Advisers Act of 1940
- Foreign Corrupt Practices Act
- Sarbanes Oxley Act of 2002 (“SOX”)
- State ‘Blue Sky’ Laws

# What has been done until now in light of the Crisis?

- **Increased focus on enforcement measures**
  - Much more use of, and massive fines for violations of the Foreign Corrupt Practices Act (FCPA)
  - sweeping expansion of ongoing investigations into market manipulation in the securities of financial institutions, esp. hedge fund managers, broker-dealers, and institutional investors – many investigations begun and lawsuits filed/charges brought (with the DOJ- Dept of Justice)
  - Also more pursuing cases of insider trading, both in the US and globally (US nexus)

## More enforcement, examples (although view that still not enough)

- Sweeping enforcement measures against market manipulation & fraud contributing to subprime crisis; 50 pending investigations in subprime area
- Largest settlements in SEC history for investors buying auction rate securities from Citigroup, UBS, Wachovia, Merrill Lynch, RBC capital, and Bank of America, inter alia
- Suits against mortgage brokers for pushing homeowners into risky & unsustainable subprime mortgages
- Suits against Wall Street brokers for defrauding customers when making \$1 B in unauthorized purchases of subprime related securities
- Charged Fannie Mae & Freddie Mac with accounting fraud, had to pay over \$450 M in penalties to settle SEC charges

# Action item focus: FCPA enforcement

- The Foreign Corrupt Practices Act of 1977 ("FCPA") generally prohibits U.S. companies & citizens, foreign companies listed on a U.S. stock exchange, or any person acting while in US, from corruptly paying or offering to pay, directly or indirectly, money or anything of value to a foreign official to obtain or retain business ("**Antibribery Provisions**")
- Also requires "issuers" (any company including foreign companies) w securities traded on US exchanges or SEC reporting to keep books & records to accurately reflect business transactions & maintain effective co go internal controls ("**Books and Records and Internal Control Provisions**")

# FCPA

- Jointly enforced by DOJ & SEC (high level of coordination on many matters, incl. Insider Trading & market manipulation)
- Proof of US territorial nexus not required for FCPA to be implicated, & FCPA violations can, & often do, occur even if prohibited activity takes place entirely outside of US
- For this reason, business leaders must be knowledgeable about all business activity, incl. activities 1000s of miles away from corp headquarters = major impact on European firms & their compliance depts

# FCPA – scope & fines

- Massive increase in scope of investigations (both US and non-US cos) and fines, plus more likely to go after foreign companies:
- Dec 08- Siemens – US\$1.6 billion in joint US/German fines (US\$800 million, largest FCPA penalty ever- a sign of things to come)
- Jan 09 Halliburton pays \$559 million fine to end an investigation of former sub for Nigerian corruption (\$382 million to DOJ & \$177 million to SEC)
- Many others, both US and int'l cos



# Why more FCPA enforcement now?

Former US AG John Ashcroft in recent major speech, cited following why current political climate creates increased opportunities & momentum for enforcement :

- Heightened international awareness of human cost of corruption as evidenced by international treaties addressing corruption (OECD, et al.) & new signatories to them;
- Economic urgency created by global economic downturn & possibility of more whistleblower & “disgruntled competitor” reports of corruption/misconduct;
- Climate of distrust of financial services & business community & related appetite for uncovering / punishing corporate wrongdoing;
- Post 9/11 cooperation between States to control flows of \$\$\$ to terrorist organizations conditions them to cooperate in other multinational investigations (definitely true w US/Euro cooperation)

## FCPA – part of US/global anti-corruption campaign

- DOJ: “Through international instruments like the OECD convention and the UN convention against corruption, ***we have seen our international partners significantly step up their anti-corruption efforts.*** Everything we're seeing suggests that this trend will continue..... We are now working with our foreign law enforcement colleagues in bribery investigations to ***a degree that we never have previously.*** In the past, in a case of joint jurisdiction between the United States and another country, it was typically the case that only the U.S. prosecution would succeed. That is now significantly less likely to be the case.”

# Action item: IFRS-US GAAP Convergence & Roadmap

- Marked change from US/SEC point of view in decades past
- Approximately 1,150 of the 12,000 companies registered with the SEC are non-US companies
- Incredible amount of cooperation between SEC, IASB, CESR, and mainly European securities regulators to make it happen
- Plan, by 2014 to eventually permit full interchangeability between US GAAP and IFRS/IAS on US capital markets, such that US companies could opt to only prepare accounts in IFRS/IAS
- Goal of seamlessly integrated EU, US capital markets
- Global crisis has highlighted need for this- greater push now

# IFRS-US GAAP Convergence & Roadmap

- NOW: Foreign registrants may submit financial statements that conform to US GAAP or (since March 2008) financial statements that conform to International Financial Reporting Standards as adopted by the IASB (that is, not jurisdictional adaptations of IFRSs), w/o need to provide US GAAP reconciliation
- Alternatively, foreign registrants may submit financial statements w national GAAP or jurisdictional adaption of IFRSs (such as IFRSs as adopted by EU), but then reconciliation of earnings/net assets to US GAAP figures required
- Convergence of accounting standards is one among many issues in the G-20 progress report & declaration- focus in Pittsburgh- 24/25 Sept. 2009

# SEC reaction to crisis: various corporate governance (co go) reforms

- In May 09, proposed comprehensive series of reforms to facilitate SH rights to nominate directors on corporate boards
- Why? W Crisis many question whether boards truly held accountable for decisions, including whether they exercise appropriate oversight of mgmt, are appropriately focused on SH interests, & whether they need to be held more responsible for such decisions
- Would provide SHs w meaningful ability to exercise state law rights to nominate corp directors; SHs who otherwise are provided opportunity to nominate directors at SH meetings would be able to have their nominees incl. in corp proxy ballot
- SHs would also have ability to use SH proposals to modify corp nomination procedures or disclosure about elections (if OK under applicable laws)

# Executive Pay & Shareholder (SH) Voting

- Among other Corp Gov efforts, on 1 July 09, SEC proposed requiring public cos receiving \$\$\$ from Troubled Asset Relief Program (TARP) to provide a SH vote on exec. pay
- Also voted to propose better disclosure of exec. compensation at public cos
- Approved NYSE rule change to prohibit brokers from voting proxies in corp elections w/o instructions from the customers
- Connected w Emergency Economic Stabilization Act of 2008 (last fall): requires SH approval of exec. compensation during period in which any obligation arising from financial assistance provided under TARP remains outstanding

# Increased regulation of “Short selling”

- Practice of selling securities borrowed from a third party w intention of buying identical assets back at later date to return to lender; short sellers hope to profit from decline in value of assets between sale and repurchase
- Sep. 08- temporary 3 wk ban against short-selling (bx of role in dangerous market volatility), although unclear if had positive effect on balance
- In Aug. 09 SEC proposed “alternative uptick rule”- allowing short selling only at an increment above national best bid (limits chance to really profit)

# Possible Prohibition of Flash Traders & Action against Dark Pools

- 18 Sept. 2009, SEC proposed banning “flash orders”, which give certain large traders sneak peeks at market activity
- Ability to freeze a buy/sell order on an exchange for up to half-second, see direction of the market
- First of several rules aimed at changing structure of stock markets (remove unfair advantages to large short-term traders vis-à-vis long-term investors)
- Dark pools: trading on private electronic markets may pose “emerging risks,” (non-transparent) SEC may require more disclosure/information on transactions-- traders w access to the private markets’ pending orders may gain unfair advantage



# SEC: new Division of Risk, Strategy & Financial Innovation (16 Sept. 2009)

- Needed by *“the derivatives revolution, the rise of hedge funds & institutional investors, technological change, & other factors have transformed both capital markets & corporate governance.”*
- combines Office of Economic Analysis & Office of Risk Assessment, plus new duties:
  - strategic & long-term analysis
  - identifying new developments/trends in financial markets & systemic risk
  - making recommendations as to how these new developments & trends affect SEC regulatory activities
  - conducting research & analysis to support SEC work
  - providing training on new developments & trends, etc.

# SEC new regulation of hedge funds

- SEC Chairman Mary Schapiro (on 17 Sept 09) predicted that any new regulation of hedge funds will likely require detailed disclosure to regulators, but not necessarily as much disclosure to the public
- Acknowledged that in some instances, such as dealing with hedge funds, it can be hard to strike balance between informing investors w/o disclosing too much about firms' trading strategies
- If proposed legislation by Congress to require hedge-fund advisers to register with SEC enacted, she predicted that final regulations will result in "fairly detailed reporting to regulators and some level of public reporting to investors."

# New Oversight of Credit Rating Agencies

- SEC announced on 17 Sept. 2009 a more demanding regs for credit rating agencies, *inter alia*:
- Adopted rules to provide more info on ratings histories - & to enable competing credit rating agencies to offer unsolicited ratings for structured finance products, by granting access to necessary underlying data
- Proposed amendments to strengthen compliance programs through requiring annual compliance reports & enhance disclosure of potential sources of revenue-related conflicts
- Adopted amendments to rules & forms to remove certain references to credit ratings by nationally recognized statistical rating organizations (**ergo, forcing parties to do more of their own due diligence/"heavy lifting", less dependence on credit ratings**) & reopened process for proposals to eliminate references to credit ratings from certain others

# SEC ratings efforts

- Finally, proposed new rules requiring disclosure of info including what a credit rating covers & any material limitations on rating scope & whether any "preliminary ratings" were obtained from other agencies – i.e., whether there was "**ratings shopping.**"

## Some other SEC plans relating to Crisis

- Proposed surprise exams by independent public accountants on investment advisors re: client accounts
- Third-party reviews of investment advisers client asset accounts
- Streamline handling complaints & tips, especially intake procedures to remedy significant problems (see Madoff)
- Increase in whistleblower programs to reward substantial evidence about significant violations (incl. \$\$\$)
- Conducting risk-based examinations of financial firms
- Improving fraud detection techniques for SEC examiners
- Expanding and targeting training
- Seeking more resources and funding to hire more examiners,
- Etc.

# Executive Pay Governance

- “Corporate and Financial Institution Compensation Fairness Act of 2009”, passed House of Reps in July, in Senate committee
  - Key corporate governance points regarding executive pay, golden parachutes, compensation committee independence, and favoring risk-adverse compensation packages at financial institutions
  - Remains to be seen what exemptions to be given for non-US entities under SEC implementing regs (currently seem applicable to dual-listed cos)

# Annual Shareholder Approval of Executive Compensation-

- `(1) ANNUAL VOTE- Any ....authorization...for an annual meeting of the shareholders to elect directors ... **shall provide for a separate shareholder vote to approve the compensation of executives as disclosed ...**

The shareholder vote **shall not be binding** on the issuer or the board of directors ...nor to create or imply any additional fiduciary duty by such board, nor shall such vote be construed to restrict or limit the ability of shareholders to make proposals for inclusion in such proxy materials related to executive compensation.

## (2) SHAREHOLDER APPROVAL OF GOLDEN PARACHUTE COMPENSATION-

- `(A) DISCLOSURE- In any [meetings]....at which shareholders are asked to approve an acquisition, merger, consolidation, or proposed sale or other disposition of all or substantially all the assets of an issuer, the person making such solicitation shall disclose in the proxy or consent solicitation material, in a clear and simple form in ... **any agreements or understandings that such person has with any named executive officers of such issuer**...concerning any type of compensation (whether present, deferred, or contingent) that is based on or otherwise relates to the acquisition, merger, consolidation, sale, or other disposition ... and the **aggregate total** of all such compensation that may (and the conditions upon which it may) be paid or become payable to or on behalf of such executive officer.



- `(B) SHAREHOLDER APPROVAL- Any proxy or consent or authorization relating to the proxy or consent solicitation material containing the disclosure ... shall provide for a **separate shareholder vote to approve such agreements or understandings and compensation as disclosed**, unless such agreements or understandings have been subject to a shareholder vote ... A vote by the shareholders **shall not be binding on the issuer** or the board of directors of the issuer or the person making the solicitation ....
- `(3) DISCLOSURE OF VOTES- Every institutional investment manager ... shall report at least annually how it voted on any shareholder vote ....

## **SEC. 3. COMPENSATION COMMITTEE INDEPENDENCE.**

- Requires new independence standards Relating to Compensation Committees-
- `(b) Independence of Compensation Committees-
- `(1) IN GENERAL- Each member of the compensation committee of the board of directors of the issuer shall be independent.
- `(2) CRITERIA- In order to be considered to be independent for purposes of this subsection, a member of a compensation committee of an issuer may not, other than in his or her capacity as a member of the compensation committee, the board of directors, or any other board committee accept any consulting, advisory, or other compensatory fee from the issuer....

## SEC. 4. ENHANCED COMPENSATION STRUCTURE REPORTING TO REDUCE PERVERSE INCENTIVES.

- (a) Enhanced Disclosure and Reporting of Compensation Arrangements-  
...Federal regulators jointly shall prescribe regulations to require each covered **financial institution** to disclose to the appropriate Federal regulator the structures of **all incentive-based compensation arrangements** offered by such covered financial institutions sufficient to determine whether the compensation structure--
  - (A) is aligned with sound risk management;
  - (B) is structured to account for the time horizon of risks; and
  - (C) meets such other criteria as .... appropriate to reduce unreasonable incentives offered by such institutions for employees to take undue risks that--
    - (i) could threaten the safety and soundness of covered financial institutions; or
    - (ii) could have serious adverse effects on economic conditions or financial stability.

- (b) Prohibition on Certain Compensation Arrangements- ...appropriate Federal regulators shall jointly prescribe regulations that prohibit any incentive-based payment arrangement....that the regulators determine encourages inappropriate risks by covered financial institutions that--
  - (1) could threaten the safety and soundness of covered financial institutions; or
  - (2) could have serious adverse effects on economic conditions or financial stability.

## Federal courts: look for increasing criticism of SEC and relationship with banks/corporations

- Last week, Fed. Judge Jed Rakoff scathingly rejected SEC's \$33 million settlement with the Bank of America regarding "materially lying" by failing to disclose to BofA shareholders the billions of dollars in bonuses owed to Merrill Lynch employees (when negotiating last year's takeover)
- ...*"does not comport with the most elementary notions of justice and morality, in that it proposes that the shareholders who were the victims of the banks alleged misconduct must now pay the penalty for not misconduct"*.
- Suggests high-profile civil cases & fines against banks/cos are not enough (mere political point scoring), that increasingly need to pursue executives & their lawyers if need be (seems Treasury officials knew anyway)
- Worth paying attention to the trial in February

# Looking down the line

- As mentioned, many expert US commentators ( both lawyers, economists & financial experts) are not convinced deep & significant changes will be made to capital markets & financial/banking system, no matter what good political rhetoric is provided for now
- *They say this will be increasingly true as markets and overall general economy in US slowly improves*
- Also, view that Wall Street will successfully use its extensive 'bipartisan' political power to frustrate real change/reforms (will accept mere window dressing)
- Despite announcements of ramped-up investigations of widespread mortgage fraud and dubious investment products blamed for causing global economic collapse, few high profile cases have so far been pursued

# Looking down the line

- So far, the only such criminal case involves two former Bear Stearns hedge fund managers; on civil side most noteworthy case is securities fraud case against Angelo Mozilo, former CEO of mortgage lender Countrywide and 2 executives.
- Says Prof. Steven Ramirez of Loyola University of Chicago School of Law, *“The perp walk has been remarkably absent during this crisis, I don’t think it’s because of a lack of criminal activity.”*
- However, the Financial Crisis Inquiry Commission, a new congressional committee has been set up & promises extensive investigations into causes of last year’s sudden crisis

# Looking down the line

- In mid-Sept. 09 Senate Judiciary Subcommittee on Crime & Drugs considering contentious & growing issue in securities law: whether to allow civil lawsuits against cos that might have aided or abetted fraud
- Third parties have enjoyed civil immunity in most sec fraud cases since decision in 2008 Supreme Court *Stoneridge Investment* case limited class actions against potential defendants like accountants, credit-rating agencies, & lawyers — leaving government to pursue them
- Sen. Arlen Specter is sponsoring legislation that would override Court's decision, permitting civil suits against anyone who "knowingly or recklessly provides substantial assistance" to someone engaged in fraud
- Could lead to massive increase in liability - argument is SEC can't handle number of cases



# US and the G-20 coordinated plans

- Moving target, worth paying close attention in coming months (24/25 Pittsburgh, US meeting)
- Covers host of issues related to global crisis:
  - Convergence of accounting standards
  - credit rating agencies
  - corporate governance (including board oversight of risk & compensation)
  - executive compensation (a favorite of Sarkozy)
  - countercyclical measures
  - prudential regulation
  - regulation of systemically significant institutions
  - non-cooperative (tax) jurisdictions, & more

# Thank you for your attention

- If you have addition questions, you may reach me at:
- [Patrick.omalley@interpresas.com](mailto:Patrick.omalley@interpresas.com)