Simpson Thacher

Regulatory and Enforcement Alert

SEC Wells Submissions: A New Caution Required?

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On November 4, 2019, the Securities and Exchange Commission brought an enforcement action that has possible implications for the Wells process. The complaint filed by the Commission in *SEC v. Bolton Securities Corp.*[1] raises the question whether parties must consider reining in their advocacy in Wells submissions—lest such advocacy be taken as proof that potential respondents are unwilling to acknowledge wrongdoing or, in common enforcement parlance, that they "don't get it." We hope that the Commission's approach in this action is an aberration rather than a new normal—one that, in our view, would undermine one of the hallmarks of due process in the Commission's enforcement program.

The underlying case involves Massachusetts-based registered investment adviser, Bolton Securities Corp., doing business as Bolton Global Asset Management ("Bolton"). While the case itself is consistent with a long line of conflict-of-interest enforcement actions against investment advisers,[2] what is notable is the complaint's discussion about Bolton's Wells submission. In short, the Commission criticizes Bolton for "fail[ing]," in its advocacy, "to acknowledge the wrongfulness of its conduct" and "offer[ing] no assurances that it would amend its written policies and procedures so as to be reasonably designed to prevent future . . . violations."[3]

SEC practitioners have long understood that their Wells submissions may be introduced as evidence in contested proceedings.[4] But the particular use and critique of Bolton's Wells submission would seem wholly at odds with the purpose of the Wells process, which (dating back to the 1972 report of the eponymous Wells Committee, chaired by John Wells) has been to afford a potential respondent the opportunity to argue why an enforcement action is unwarranted. As then-Commissioner Paul Atkins noted in a 2007 speech: "In many ways, . . . 'Wells submissions' operate as a last clear chance for respondents to persuade the staff that an enforcement recommendation is not warranted. If that fails, the Wells submissions are submitted to the Commission, along with a staff

[1] Civil Action No. 4:19-cv-40143 (D. Mass. filed Nov. 4, 2019) (available at https://www.sec.gov/litigation/complaints/2019/comp24660.pdf).

[2] The Commission sued Bolton for, among other things, (i) failing adequately to disclose that the mutual fund share classes that Bolton was advising its clients to buy or hold were paying 12b-1 fees to Bolton's broker-dealer affiliate (notwithstanding the availability of less expensive share classes, with no 12b-1 fees, from the same mutual funds); and (ii) engaging in principal trading transactions with clients through its affiliated broker-dealer without giving the clients proper disclosure or obtaining their consent. *Id.* (¶¶ 1 & 2).

[3] *Id.* (¶¶ 41-43).

[4] *See* SEC Form 1662 (Supplemental Information for Persons Requested to Supply Information Voluntarily or Directed to Supply Information Pursuant to a Commission Subpoena (available at https://www.sec.gov/files/sec1662.pdf) ("The staff of the Commission routinely seeks to introduce [Wells] submissions . . . as evidence in Commission enforcement proceedings, when the staff deems appropriate.").

recommendation memorandum, so respondents are assured that the Commission has both sides of the story when it considers a recommendation in a contested matter."[5]

To judge a party insufficiently remorseful—or unwilling to change its approach in the future (and therefore deserving of an injunction)—on the basis of the party's Wells submission is to turn the purpose of the Wells process on its head: from the robust advocacy and legal and factual argumentation that are so critical to ensuring fairness in an enforcement process to something much more restrained. If the Commission wishes to hear "both sides of the story," parties should not have to fear that their Wells submissions will be taken as evidence that they are unwilling to acknowledge wrongdoing and are at risk of repeating that wrongdoing in the future. The predicament *Bolton* creates for potential respondents is made even more acute by the Commission's policy that admissions made in Wells submissions may be used in contested proceedings brought by the Commission.[6] (It is also worth noting, in this regard, that Wells submissions are discoverable by third parties. Thus, the ramifications of such admissions may well go beyond the Commission process itself.)

While the Third Circuit's recent decision in *SEC v. Gentile*[7] makes clear that "federal courts may not grant SEC injunctions except 'upon a proper showing of the likelihood of future harm,'"[8] we would urge that the Commission generally refrain from invoking Wells submission advocacy when seeking to clear that hurdle. The Commission's approach in *Bolton*, to the extent it is repeated, will have a chilling effect on Wells submissions, and will certainly undermine the Wells process as it has existed and benefitted the Commission for nearly half a century. We are hopeful that *Bolton* is an exception and does not represent a new rule for the Wells process going forward.

[5] Commissioner Paul S. Atkins, Remarks at the Eighth Annual A.A. Sommer, Jr. Corporate, Securities and Financial Law Lecture (Oct. 9, 2007) (available at https://www.sec.gov/news/speech/2007/spch100907psa.htm).

[6] *See* Enforcement Manual, SEC Division of Enforcement (Nov. 28, 2017) (available at https://www.sec.gov/divisions/enforce/enforcementmanual.pdf) at Section 2.4 ("[A]ny Wells submission may be used by the Commission in any action or proceeding that it brings. . . . The staff may reject a Wells submission if the person making the submission seeks to limit . . . its admissibility under Federal Rule of Evidence 408."); *see also supra* at n.3.

[7] No. 18-1242 (3rd Cir. Sept. 26, 2019) (slip op.) (available at https://www2.ca3.uscourts.gov/opinarch/181242p.pdf).

[8] *Id.* at 20 (quoting *SEC v. Commonwealth Chemical Securities, Inc.*, 574 F.2d 90, 99 (2nd Cir. 1978)).

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