

Overseas Cos. Are Well Within Reach Of SEC Enforcement

By **Eugene Goldman** (September 23, 2022, 5:53 PM EDT)

It is not uncommon for the U.S. Securities and Exchange Commission, in connection with an investigation, to approach individuals and entities based overseas to produce documents and be interviewed in their country.

Their first inclination may be that there is nothing to worry about because they are beyond the reach of the SEC. However, by not agreeing to cooperate, these individuals and entities may be compelled by the securities regulator in their own country to attend an interview and produce documents for onward delivery to the SEC.



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We have experienced situations where the interview, whether or not given voluntarily, opens with a statement by the host regulator, then all the substantive questions to follow are posed by the SEC enforcement staff visiting that jurisdiction.

This type of overseas fact-gathering by the SEC is the result of the SEC's development of a sophisticated cooperative mechanism via bilateral and multilateral cooperation agreements with regulators around the world. The mechanism requires defense counsel to have a clear understanding of the ground rules and devote ample time for preparation with clients who are unfamiliar legally and culturally with the staff's reputation for aggressiveness.

SEC international enforcement has matured in recognition that investor schemes and market abuses often do not stop at a country's border.

With modern technology and rapid trading data and asset movements, such conduct is often carried out far from the suspected perpetrator's location. That requires the regulators to gather information from third parties, such as banks, investment firms, accountants and custodians, and disclose the identity of traders and their trading activity with accounts abroad.

Whether suspected violations involve fraudulent offerings of unregistered securities, false financial reporting, deficient auditing, corrupt payments or insider trading, it is fair to conclude that the SEC has been able to duplicate outside the U.S. many of the investigative requirements imposed on those in the U.S.

The SEC enforcement staff recently acknowledged, in charging 18 defendants in an international stock manipulation scheme, the assistance of 15 named overseas authorities. Nekia Hackworth Jones, director

of the SEC's Atlanta regional office, said that "As this case demonstrates, the Division can uncover misconduct even when it crosses borders and is concealed behind multiple layers of obfuscation." [1]

Evidence of the SEC's receipt of assistance from foreign regulators is found from an array of SEC litigation releases in which the SEC thanks by name an overseas regulator — often more than one.

We have examined over 40 enforcement actions since 2018 where the SEC has publicly acknowledged the assistance of specific overseas regulators. Information about these actions is described below. In addition, cooperation is not a one-way street — in response to its receipt of hundreds of requests for assistance annually, the SEC uses its tools to gather and provide important information to overseas regulators.

The expanding global reach of the SEC can affect compliance personnel at foreign subsidiaries of U.S.-listed companies. In-house detection of suspected overseas activity can prompt local compliance to bring it to the attention of its parent's management, which then may report it to the SEC, its home regulator. The SEC may, in turn, seek the assistance of its overseas counterpart to gather information from local sources who may have knowledge about the suspected activity.

Cooperation between the home regulator and the regulator where the suspect activity has taken place helps combat the scheme and may generate information that permits the taking of appropriate personnel action and systems reviews.

Increased Cooperation and Assistance

The escalation of foreign interdependence cuts through successive U.S. administrations.

In November 2008, SEC Chairman Christopher Cox, in his last speech on the topic before leaving the SEC, noted that the "scale of our international enforcement cooperation has been massive [and over] the last year, the SEC made 556 requests of foreign regulators for assistance ... [and] received 454 requests from foreign regulators for this kind of law enforcement help." [2]

Then followed then-President Barack Obama's budget message to Congress, boosting for the first time an SEC budget request in excess of \$1 billion for fiscal year 2010. The message noted the importance of funding the SEC's international activities. It cited a major international regulatory policy initiative to strengthen investor protection "as well as work with the Division of Enforcement on numerous cases with significant international components." [3]

By 2018, the SEC's Office of International Affairs handled more than 1,200 requests for assistance made to foreign regulators, according to the SEC's enforcement director at the time, and a third of the SEC's enforcement actions involved an international component. [4]

The SEC recently emphasized that it "continues to process increasing numbers of incoming and outgoing cross-border tips, complaints, and referrals. International enforcement is vital to the SEC's investor protection mission." [5]

IOSCO's Multilateral Memorandum of Understanding

The SEC's primary mechanism for obtaining evidence from and providing evidence to foreign securities regulators has been the International Organization of Securities Commissions' multilateral

memorandum of understanding, or MMOU, concerning consultation and exchange information.

IOSCO is the primary international association of securities regulators dedicated to promoting high standards of securities regulation and the integrity of the markets by effective enforcement against offenses.[6]

The MMOU currently has over 125 signatories.[7] The MMOU is not an international treaty. It is ultimately a form of soft law, as it is not binding on the parties. Despite its nonbinding status, it is followed in the interests of fostering the fair confidence in the securities markets by enabling its signatories to obtain information from outside their jurisdiction and undertake cross-border investigations of possible violations of the securities laws.

Academic research by Roger Silvers, an adjunct assistant professor at the University of Utah, indicates that IOSCO membership fosters equity liquidity and market integrity and that SEC enforcement of U.S.-listed foreign firms "is around three times as likely when the firm's home country regulators are linked to the SEC by the MMoU." [8]

Becoming a signatory to the MMOU requires a review of submitted information on whether the applicant-regulator's country has laws in place that comply with IOSCO's objectives and principles of securities regulation. These principles include that the regulator has comprehensive investigation and enforcement powers, works under an effective regulatory system and has the authority to share information with foreign counterparts.[9]

Requests for assistance under the MMOU require the SEC to submit detailed information to the requested authority describing, among other items, the entities and individuals involved, whether they are regulated, the type of scheme, the nature of the suspected misconduct, and location of assets.

The requests also need to describe information that may be useful to the SEC, such as sources of information and identification of persons from whom statements are needed.

Assuming the requested authority is satisfied with the submission of the required information and depending on facts and circumstances, the requested authority will provide the SEC documents and data it has in its files that relate to the subject matter of the request, require the production of documents from any person designated by the SEC and compel the taking of testimony.[10]

Enhanced Multilateral Memorandum of Understanding

IOSCO established the enhanced MMOU in 2016 to provide additional key powers IOSCO identified as "necessary to ensure continued effectiveness in safeguarding market integrity and stability, protecting investors and deterring misconduct and fraud." [11] It took this action to keep pace with technological developments, increased globalization of the financial markets and how violations occur.

The expansion of assistance includes obtaining and sharing of audit work papers and other information relating to the audit or review of financial statements; asset freezes; emails, credit card and telephone records, with the assistance of a prosecutor, court or other authority; and recordings of telephone conversations maintained by regulated persons and entities.

Over 20 of the signatories of the MMOU have signed onto the enhanced MMOU, including authorities in Singapore, Israel, Brazil and the Bahamas.

In addition, IOSCO responds to changes in global market conditions and issues as they develop. For example, it is noteworthy that in July IOSCO issued its crypto-asset road map, with the SEC, the U.S. Commodity and Futures Trading Commission and over 20 other members serving on a fintech task force. Its focus is on analyzing and responding to market integrity and investor protection concerns within the crypto-asset space.[12]

Survey of Enforcement Actions

The SEC publicly acknowledged receiving assistance from one or more of its overseas counterparts in over 40 enforcement actions filed since 2018.

From our review of these actions, many cases included foreign primary defendants, relief defendants, foreign brokerage accounts, nominees and shell companies, as well as alleged Foreign Corrupt Practices Act violations, microcap and pump-and-dump schemes, illegal coin and token offerings, a crypto lending platform's improper transfer of funds to digital wallet addresses, and insider trading.

Several did not allege fraud but rather stand-alone unregistered securities violations and erroneous order-marking information in violation of Regulation SHO.

By way of illustration, in its first cryptocurrency-related litigation, the SEC thanked the Cayman Islands Monetary Authority; the Hong Kong Securities and Futures Commission; the Monetary Authority of Singapore; the Ontario Securities Commission; the Romanian Financial Supervisory Authority; and the Thailand Securities and Exchange Commission for their assistance in the investigation that led the SEC to bring an action against an online crypto lending platform, BitConnect, its founder Satish Kumbhani, and various promoters.[13]

The SEC charged that defendants conducted a fraudulent and unregistered offering and sale of securities in the form of investments in a so-called lending program that ultimately succeeded in obtaining more than \$2 billion from investors worldwide, including the U.S.

The SEC alleged that BitConnect and Kumbhani siphoned off investors' funds off for their own benefit by transferring those funds to digital wallet addresses controlled by Kumbhani and various promoters.

Kumbhani was later indicted[14] and reportedly recently arrested by the Indian authorities.[15] So far, the SEC obtained judgments against two promoters, including Michael Noble and a relief defendant for more than \$3.5 million and 190 bitcoin.[16]

Practical Considerations and Need for Preparation

As shown above, for foreign firms and individuals operating in many countries outside the U.S., being far from the U.S. geographically should provide little comfort that questionable activities affecting U.S. investors are safe from SEC scrutiny.

Foreign witnesses and producers of emails and other documents are not familiar with the tenacity and level of scrutiny of an SEC investigation. Interrogations can last more than one day, and document demands are detailed yet broad, including demands for financial and auditing materials, emails and other electronic documents.

It is thus critical for overseas subjects of SEC requests for information to understand:

- The SEC's powers, jurisdiction and rules of practice;
- Privileges and other rights of those from whom the SEC is seeking information via the foreign regulator;
- How to narrow the scope and challenge the foreign regulator's adherence to the SEC's requests;
- The necessity of thorough preparation and types of review needed; and
- How to secure confidentiality treatment of the furnished information pursuant to Section 24(d) of the Securities Exchange Act, which exceeds Freedom of Information Act protections, and declarations from the requested authority that, under its laws, such as the U.K.'s Financial Services and Markets Act, the documents transferred to the SEC are confidential.

Practically, we have found it helpful to save the mental energy of testifying clients whose first language is not English by arranging the services of a translator to at least translate the questions, and to use the resources of our overseas colleagues as a home base where the clients reside.

Conclusion

As suspect payments, false disclosures and trading schemes metastasize and seep across borders, the SEC has become the chief participant in a robust international enforcement network. MMOU and enhanced MMOU usage have matured, and more countries continue to sign on. Those overseas and their counsel will face continuing challenges navigating through SEC investigations and interactions with the SEC staff via the MMOU process.

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[1] <https://www.sec.gov/news/press-release/2022-145>.

[2] <https://www.sec.gov/news/speech/2008/spch110708cc.htm>.

[3] <https://www.govinfo.gov/content/pkg/BUDGET-2010-APP/pdf/BUDGET-2010-APP.pdf>.

[4] <https://www.sec.gov/news/speech/speech-peikin-120318>.

[5] The SEC Office of International Affairs materials, The SEC Speaks in 2022.

[6] https://www.iosco.org/about/?subsection=about_iosco.

[7] <https://www.iosco.org/about/?subSection=mmou&subSection1=signatories>.

[8] <https://reader.elsevier.com/reader/sd/pii/S0165410120300033?token=BC5614250ED7300E71E7015404E140D3AA23E86720BCF9847B5D10659C78C55EC7855F3808F60E5829CB44DD6E78B4C3&originRegion=us-east-1&originCreation=20220908143757>.

[9] <https://www.iosco.org/about/pdf/High-Level-Questionnaire.pdf>.

[10] <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD386.pdf>.

[11] <https://www.iosco.org/about/?subsection=emmou>.

[12] <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD705.pdf>.

[13] <https://www.sec.gov/news/press-release/2021-172>.

[14] <https://www.law360.com/articles/1468649/bitconnect-founder-indicted-in-2b-ponzi-scheme-feds-say>.

[15] <https://news.coincu.com/118923-india-wants-bitconnect-boss/>.

[16] <https://www.sec.gov/litigation/litreleases/2021/lr25177.htm>.