

SEC INVESTIGATIONS

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I. Introduction

Almost every public company in America has been, at one time or another, involved with a Securities and Exchange Commission (Commission or SEC) investigation either as a subject or a witness. Handling such an investigation is like steering a course between the devil and the deep blue sea. The course can be navigated only with an in-depth knowledge of the enemy and the rules by which he plays. This article explores the legal rights of targets, subjects, and witnesses in SEC investigations, as well as the SEC's Rules Relating to Investigations.

Additionally, this article compares the current state of the law with the changes proposed by the American Bar Association Section of Corporation, Banking, and Business Law's Federal Regulation of Securities Committee ("Task Force") in its "Report of the Task Force on SEC Rules Relating to Investigations" ("Task Force Report").ⁱ The Task Force Report charged that the Commission's existing rules regarding investigations "are in many cases, inadequate" to ensure that witnesses and subjects are treated fairly. Therefore, the Task Force has proposed a number of rule changes that would safeguard a witness's rights without unduly jeopardizing the public interest in enforcement of the securities laws. Indeed, to underscore this point, the Task Force's proposed rules contain a provision that violations of the rules do not constitute a defense to a judicial or administrative proceeding, except in a proceeding to enforce a subpoena during the course of an investigation.

The changes to the SEC's Rules Relating to Investigations (17 C.F.R. § 203 *et seq.*) proposed by the Federal Regulation of Securities Committee in its Task Force Report, have not been adopted. Indeed, it is fair to say that the Commission and its staff have virtually ignored the Task Force Report. The Task Force Report had recommended various changes in the SEC's Rules, including (1) extending the SEC's Rules Relating to Investigations to informal inquiries; (2) requiring that the SEC orders of investigation be more specific; (3) limiting formal orders of investigation to one year; (4) requiring greater specificity in SEC formal orders and subpoenas; (5) permitting a challenge to an investigative subpoena at the administrative level; (6) expanding the right of a witness to purchase copies of his testimony, the exhibits, and documents referred to during the investigative testimony; (7) requiring the SEC to notify participants in an investigation of its outcome; (8) notifying targets of their status; and (9) eliminating the Commission's sequestration rule.

II. Informal Inquiries

Each of the statutes administered by the Commission authorizes SEC investigations.ⁱⁱ A Commission investigation can begin as a result of a complaint from the public or from a state or federal agency, a reference from another Commission division, or a review of the Commission's files. Market surveillance, informers, industry contacts, and official curiosity are also sources.ⁱⁱⁱ In the Sporkin era, one source of investigations was the newspaper. In fact, during the foreign corrupt practices investigations, SEC staff attorneys regularly spent a portion of each morning reviewing *The Wall Street Journal* and the business sections of *The New York Times* and *The Washington Post*.

Normally, when a complaint is received, the staff conducts an informal or preliminary inquiry. No process will issue and the staff will seek voluntary information. They might

telephone participants or their counsel and ask for information or for the voluntary production of documents. In addition, the staff might send out questionnaires, “blue sheets,”^{iv} interrogatories, or letters seeking voluntary information. At this stage, the staff may not swear witnesses or compel testimony through the issue of Commission subpoenas,^v but they may ask that participants appear for interviews or give sworn testimony before a notary public.

Although the procedural protections set out in the SEC’s Rules Relating to Investigations^{vi} do not apply to informal inquiries, as a practical matter the Commission’s staff normally affords a witness the full range of procedural rights he would have had if a formal investigative proceeding had been instituted. The Task Force Report has suggested that the Commission should formalize this practice by extending to informal inquiries those procedural protections currently applicable to formal Commission investigations. The Task Force argues that an informal inquiry is equally as coercive as a formal investigation; and, consequently, the Rules Relating to Investigations, which are meant to promote fairness, should apply to both.

Informal inquiries have tended to become more drawn-out. In fact, it is not unusual for the SEC staff to conduct its entire investigation in an informal setting without obtaining a formal order. Indeed, an investigation may proceed from informal inquiry to an enforcement recommendation without a formal order being issued. The reason for this trend is that subjects of Commission inquiries often choose to comply voluntarily with an informal inquiry in order to avoid the thorny question of whether disclosure of a formal order of investigation must be made.

Given this trend and the SEC staff’s practice of affording witnesses the procedural rights they would have had if a formal investigative proceeding had been instituted, the Task Force’s recommendation is appropriate. The proposed amendment also would serve as a

constant reminder to staff attorneys of the rights of a witness without unduly impairing the Commission's ability to investigate.

III. Formal Investigations

The Commission may order a formal inquiry if it deems it necessary.^{vii} A formal inquiry is commenced by the Commission's issuance of a formal order of investigation. Probable cause is not a prerequisite for the issuance of such a formal order.^{viii} Upon issuance of the formal order, the staff may invoke the Commission's subpoena power.

Normally, once an informal inquiry has come to an impasse, the SEC staff requests a formal order from the Commission to develop the inquiry further through use of subpoena power. The staff does this by preparing a memorandum to the Commission showing that the SEC's preliminary inquiry has revealed possible violations of the securities laws or has raised questions about a particular transaction. In this memorandum, the staff explains how a formal order will assist the investigation's progress. When issued, the formal order designates officers who are empowered to administer oaths, to subpoena witnesses, and to require the production of documents.^{ix}

In order to obtain subpoena power, the SEC staff will request a formal order when the participants refuse to cooperate voluntarily with an informal inquiry. Therefore, defense counsel should consider the ramifications of adopting a stone-wall defense when met with the Commission's initial request for information. Voluntarily providing information may satisfy the staff's curiosity and avoid entanglements in a full-blown investigation. It is a truism that once a Commission investigation is under way, it is difficult for the bureaucracy to put it to rest without showing some results. This is not to say, however, that cooperation is always warranted at this

stage. If counsel's own preliminary investigation reveals that his client has culpability, he may decide that a stone-wall defense is the best means of distancing or delaying the Commission's investigation. Furthermore, if an individual or corporation that is subject to an informal inquiry believes its rights are being abused by the staff's invasion of privilege or otherwise, the investigation should be transformed into a formal proceeding.

IV. Formal Orders

When the Commission decides to investigate a matter based upon the staff's recommendation, it issues a written formal order of investigation. The issuance of a formal order is solely within the Commission's discretion. A private citizen has no standing to bring an action demanding that a court compel the Commission to investigate.^x

The formal order is typically divided into three sections. Section I is the public official files section. This includes an identification or description of the named subject^{xi} disclosed in the Commission's official files, together with any other pertinent facts. Section II, the staff report section, contains information tending to show each statutory violation that may have occurred.^{xii} Section III, the purpose and order section, recites the specific violations that the staff report section shows may have occurred, directs that an investigation be made, and designates the staff members who are empowered as officers to conduct that investigation by administering oaths and subpoenaing documents. As staff turnover occurs, this section of the formal order will be amended to designate the successor staff members. When representing a witness in a Commission formal investigation, counsel should always verify that the staff attorneys and accountants in attendance have been named in the formal order.

The Task Force has charged that the Commission's formal orders tend to be couched in boilerplate antifraud language. It contends that these orders should be revised to contain a brief description of the specific factual and legal basis supporting the Commission's belief in the existence of an actual or potential securities law violation. At present, a formal order of investigation simply commences the investigative process. Like an order empanelling a grand jury, it is not a complaint or an indictment. The Task Force Report would require the Commission's staff to plead a factual and legal basis supporting its belief that the law has been violated. This change would prohibit the Commission's staff from conducting investigations out of curiosity, as they are now permitted to do.^{xiii}

Moreover, a more narrow factual pleading may afford those parties subjected to SEC inquiries the ability to object to areas of inquiry not specified in the pleading. As currently drafted, formal orders are ambiguous, and the scope of the Commission's investigation is virtually unlimited.

Furthermore, the Task Force has proposed that formal orders expire one year after their issuance. One of the greatest problems that exists in a bureaucracy is bringing a case to a conclusion after an investment of thousands of hours of investigation. Normally, in order to close an investigation, an SEC staff attorney must prepare a memorandum explaining why closure is warranted. Quite naturally, the staff attorney finds himself in the position of having to justify why resources were expended without results. Consequently, it is easier to let an investigation drag on than to admit that the investigation was either improvident to begin with or produced no evidence of violations. An automatic cutoff date will allow an investigation to die a natural death.

Finally, under the current Rules Relating to Investigations, participants in an investigation have no absolute right to be advised as to the outcome of an investigation. While the staff occasionally will advise that an inquiry has concluded without any enforcement recommendation, at other times they have refused to do so. The Task Force Report proposes an amendment to Rule 3 of the Rules Relating to Investigations which would give persons who have testified or provided evidence an absolute right to notification of the investigation's outcome as it pertains to them.

V. Investigations Pursuant to Formal Order

After the formal order is issued, the staff determines the witnesses and documents to be subpoenaed. The commissioners are policy-makers, thus, the planning, direction, and execution of an investigation is left to the staff. The commissioners do not review the subpoenas before they are issued nor do they plot the investigation's course.^{xiv}

A formal order is interlocutory in nature and is not reviewable.^{xv} However, it has been suggested that if the Commission issues a formal order plainly beyond its statutory authority, or if the SEC threatens irreparable injury in clear violation of an individual's rights, a district court might have the authority to enjoin the Commission.^{xvi}

A Commission investigation is not a proceeding. Its sole purpose is to develop facts that may subsequently be used to determine whether the institution of an enforcement proceeding is warranted. Since a Commission investigation does not adjudicate legal rights, the due process clause does not require that the investigation be conducted like a trial.^{xvii} Therefore, the rights of appraisal, confrontation, and cross-examination do not apply.^{xviii} Yet, persons summoned are entitled to general notice of the investigation's purpose and scope.

A Commission investigation, as a grand jury investigation, is inquisitorial in nature.^{xix} It is normally conducted in private. Parties affected by the investigation do not have the right to have an attorney present at all investigatory proceedings^{xx} or to be notified when subpoenas for the party's records are issued to third parties.^{xxi} Since an SEC investigation is not governed by judicial standards, leading questions may be asked, hearsay elicited, and clues and rumors developed during the course of a witness's testimony.^{xxii}

However, certain limited rights are afforded to witnesses by the SEC's Rules Relating to Investigations.^{xxiii} Thus, upon request, a witness may inspect the Commission's formal order of investigation, may be represented by counsel during questioning, may make a statement for the record at the conclusion of his testimony, and may obtain a copy of his transcript. Although not part of its Rules Relating to Investigations, the SEC staff's practice is to advise every witness of his rights under the Fifth Amendment and the consequences of perjury or false statement. Additionally, the staff will provide a witness with a Statement of Routine Uses under the Privacy Act. These rules and the SEC staff's practice have been in place for over 25 years. In operation, they have struck a delicate balance between the interests of the subject of SEC inquiries and the public's need to investigate unencumbered by procedural delay.

Under current practice, when a witness advises the staff of his intention to assert his Fifth Amendment privilege against self-incrimination, the staff will require his attendance for testimony and to compel invocation of the privilege at that time. The Task Force Report would eliminate this practice and excuse a witness's attendance when he or his counsel advises the staff of his intention to invoke the Fifth Amendment. The Director of the Division of Enforcement or the Regional Administrator for the Region conducting the inquiry may determine that the witness's attendance is necessary.

The Commission consistently has taken the position that since its investigations are not adversarial proceedings, there are no targets of its investigations. Therefore, the SEC has refused to advise witnesses whether they are targets of inquiry. This is contrary to the practice of the Department of Justice. The Task Force Report has proposed a new Commission rule that would require a warning notice to a prospective target when the SEC has received information about a witness that, if true, would warrant the institution of a judicial or administrative proceeding by the SEC based upon violations of any statute, rule, or order that the Commission is responsible to enforce.

Any request for information, whether by subpoena or otherwise, generally comes with a transmittal letter indicating the confidential nature of the inquiry and a warning that the request should not be construed as an implication of wrongdoing. That letter will normally enclose SEC Form 1662, which is annexed hereto, entitled “Supplemental Information for Persons Requested to Supply Information Voluntarily or Directed to Supply Information Pursuant to Commission Subpoena” (September 1989). Whenever an individual is asked to supply information to the SEC or to testify, the witness is provided with this form advising him of certain rights under the Commission’s Rules Relating to Investigations, the witness’s right to make submissions, and the witness’s rights under the Freedom of Information and Privacy Acts.

VI. Right to Inspect Formal Order

Under the Commission’s Rules Relating to Investigations, a witness normally is shown the formal order of investigation at the outset of his testimony. However, the witness may not retain a copy of the formal order unless he makes a formal written request, which must be expressly approved by an official in a regional office at the level of assistant regional administrator or higher or an assistant director of the division or higher.^{xxiv}

Therefore, counsel should always present a written request for a copy of the formal order either prior to or at the time his client testifies. Although, as noted above, formal orders are drafted ambiguously, they provide counsel with some information as to the scope of the investigation and its subjects. Such information is invaluable in assisting counsel to perform his own factual inquiry and to organize his defense.

The Task Force Report proposes an expansion of this right by suggesting that all Commission subpoenas be accompanied by a notice of the recipient's right, upon written request, to receive a copy of the order of investigation in addition to any amendments or extensions. While the proposal permits the director of the SEC Division of Enforcement or the regional administrator for the region conducting the investigation to limit this right of inspection, he may do so only under a written finding that production of a copy of the order of investigation would materially hinder the investigation or otherwise would be contrary to the public interest.

VII. Right to Counsel

Rules 7(b) and 7(c) of the SEC's Rules Relating to Investigations provide that all witnesses may be represented by counsel. Such counsel may advise the witness before, during, and after the conclusion of the examination, ask clarifying questions at the conclusion of the examination, and make summary notes solely for the use of the witness. The same rules also provide for the sequestration of witnesses and their counsel, *i.e.*, a witness or his counsel cannot attend a hearing where the testimony of another witness is taken.^{xxv}

A literal application of the sequestration rule would prevent a lawyer from representing more than one witness in a single Commission investigation since, under the

sequestration rule, a lawyer for one witness may not attend the testimony of another witness. While the SEC rarely applies this rule in a literal fashion, it has done so occasionally.

The courts, which have addressed such literal applications of the rule, have held that the rule infringes upon a witness's right to choose his own counsel. In the absence of concrete evidence that the Commission's investigation would be obstructed, an attorney who has already acted as counsel for one witness may not be prevented from representing a second witness. Such an interpretation of the sequestration rule would deprive a witness of his right to freely select counsel.^{xxvi}

At least one court has held that an attorney representing a witness during a Commission investigation may have a technical adviser at his side during that witness's testimony despite the Commission's rule excluding nonlawyers from attending investigatory proceedings. The court reasoned that a client's absolute right to counsel during such a proceeding would be qualified unless counsel could receive substantive guidance from an expert technician when he determines that such assistance is essential.^{xxvii} This need for technical assistance will most often arise when an attorney is representing a witness who is an accountant, geologist, or inventor, and when the witness is being questioned about technical matters.

The Task Force Report would eliminate the Commission's sequestration provisions. It would also broaden the scope of a lawyer's participation during investigative testimony by recognizing counsel's right to object to questions and to ask additional questions that are reasonably related to the investigation.

Finally, Rule 7(e) as currently constituted provides that the Commission's staff may report "dilatory, obstructionist, and contumacious conduct" by a witness's counsel during the

course of an investigation to the Commission for appropriate proceedings against counsel under Rule 2(e) of the Commission's Rules of Practice. The Task Force has suggested deletion of this rule because it is seldom invoked and only serves to chill effective advocacy.

VIII. Right to Transcript

A witness may request a transcript of his investigative testimony, subject to the Commission's denial for "good cause."^{xxviii} Notwithstanding such a denial, the witness may inspect his transcript and make corrections to it.^{xxix} The SEC does not use stenographic reporters to transcribe investigative testimony. Instead, it has contracted with a service that either produces a transcript from a tape recording or has a reporter repeat what he hears onto a tape recording. These systems tend to be unreliable and inaccurate. Consequently, the witness should always review his transcript.

A witness may not tape record his testimony nor may he demand that the staff guarantee him the right to a copy of his testimony before submitting to interrogation. Such a guarantee would nullify the agency's right to withhold a transcript for "good cause."^{xxx}

The entire investigative hearing is not required to be transcribed under the Commission's rules, due process requirements, or the Jenck's Act.^{xxxi} The staff may go "off-the-record" during an investigative hearing.^{xxxii} However, it is prudent to keep everything on the record, or at least to summarize on the record what happened "off-the-record." From the SEC's perspective, this will avoid charges that the witness was badgered or coerced or made exculpatory statements during the "off-the-record" conversation. From the witness's counsel's perspective, improper staff conduct will be recorded as such. Rarely, but at times, an

inexperienced staff attorney will be unable to phrase a non-argumentative question or, even worse, will accuse a witness of lying without attempting to impeach him.

Currently, the SEC does not allow the witness to obtain copies of exhibits and documents referred to during his testimony when he purchases a transcript. However, a witness may succeed in obtaining these materials by forwarding a written request to an associate director in the Division of Enforcement or to the regional administrator in charge of the investigation. A witness has no absolute right to obtain these documents under the Commission's rules.

The Task Force has proposed that witnesses be allowed to purchase copies of their testimony, the exhibits, and the documents referred to during the investigative testimony unless a finding is made that it would hinder the investigation. This legitimate proposal should be adopted. There is no reason to deny a witness access to the exhibits and documents referred to during his testimony. In fact, the proposal may assist the staff in organizing its own records. If the staff is required to produce on demand all records or documents referred to during investigative testimony, it will tend to maintain a single file for the documents and transcripts. I have experienced instances when the staff during litigation following an investigation was unable to locate documents that were shown to a witness during his investigative testimony. This raises interesting questions under the Federal Rules of Civil Procedure. The implementation of the Task Force's recommendations may avoid such occurrences.

IX. Service of SEC Subpoena Within the Country

Each of the statutes enforced by the Commission empowers any member of the Commission, or any officer designated by it, to issue subpoenas requiring the attendance of witnesses and the production of documents from any place in the United States.^{xxxiii} Service of a

Commission subpoena is made by personal delivery; by leaving it at a witness's office with the person in charge or, if no one is in charge, by leaving it in a conspicuous place; by leaving it at his dwelling with someone of suitable age and discretion; by mailing it by registered or certified mail; or by any other method whereby actual notice is given prior to the subpoena's return date.^{xxxiv}

When serving the subpoena, the SEC is not required to advance fees for the witness's attendance and mileage.^{xxxv} Reimbursement may be obtained by filing a witness fee application. Therefore, at the outset of his appearance to testify, a witness should request a witness fee application from the staff attorney conducting the investigation. If the staff attorney does not have one available (and they normally do not), counsel should put his request on the record and follow the verbal request with a letter. After the fee application is filed, the witness normally must wait several months to be reimbursed. Because the Commission has been tardy in reimbursing witnesses, the Task Force proposed an amendment to Rule 6 requiring payment to the witness of the attendance fees and costs within 30 days.

X. Nationals Outside the Country

If the Commission wishes to take the testimony of a national or resident of the United States who is in a foreign country, it must seek a court order under 28 U.S.C. § 1783. Section 1783 provides that, before a subpoena can be issued, the court must find that the testimony or the production is necessary and not otherwise obtainable. If counsel is representing a witness who resides outside the United States, he should insist on the formal application procedure, rather than voluntarily producing the witness upon his return, because the application will reveal important information about the investigation. There is a risk that the application may make public information and allegations about the client. If the investigation is being followed by the

press, these allegations may find their way into the papers. The risk may be minimized, however, by requesting a protective order from the court, effectively sealing any nonpublic information developed during the course of the investigation.

Service of the subpoena under § 1783 must be effected in accordance with the provisions of the Federal Rules of Civil Procedure relating to service of process on a person in a foreign country. At the time service is effected, these witnesses must be tendered necessary travel and attendance expenses.^{xxxvi}

XI. Foreign Nationals

The Commission lacks jurisdiction to issue an investigative subpoena to a non-U.S. citizen in a foreign country.^{xxxvii} However, it may subpoena documents from abroad if service of the subpoena was made in the United States and the party served with the subpoena controls the documents to be produced.^{xxxviii}

A foreign law prohibiting disclosure of documents located in that foreign jurisdiction will not prevent the enforcement of a subpoena by a U.S. Court ordering production of the documents.^{xxxix} When faced with such foreign blocking or secrecy laws, the U.S. court will balance the competing interests involved in determining whether to order production. If production is ordered and foreign law prevents the witness's compliance, the court will determine what sanctions, if any, are appropriate based on the party's good faith efforts at compliance.^{xl}

XII. Subpoenas—Motion to Quash

An SEC subpoena, unlike a grand jury subpoena, is not self-executing. In order to obtain compliance, the Commission must apply to a federal district court for an order requiring

enforcement. A subpoenaed witness who believes he has grounds to refuse compliance must ignore the subpoena and await the Commission's institution of a subpoena enforcement action before he has a right to contest the subpoena.^{xli} There is no procedure by which a recipient of an SEC subpoena can move to quash it.^{xliii}

Therefore, a practitioner who believes a Commission subpoena is overly broad or violates some applicable privilege should, as an initial matter, contact the staff before the date set for compliance and seek to narrow the scope of the subpoena. Most often, the staff will entertain any reasonable proposal to limit the volume of documents required to be produced. Normally, the SEC staff will not press for information once the witness has demonstrated that a privilege exists. However, if negotiations fail and the staff continues to demand the documents or information, the only recourse is to refuse compliance and await the Commission's enforcement proceeding.

The Task Force made five important proposals with respect to Commission subpoenas. First, they proposed that a Commission subpoena shall be returnable within a reasonable period of time. A subpoena returnable 20 days after service is presumed to be reasonable. This change was proposed to afford a witness adequate time to consult with counsel. Attorneys practicing in this area can recite numerous instances when they have received subpoenas from the SEC staff returnable on one or two days' notice. This proposed amendment will put an end to this practice.

Second, the Task Force Report proposed that any documents listed in the subpoena be described with particularity. This change was proposed to eliminate blunderbuss subpoenas that demand every record ever generated by the witness. The requirement will force staff attorneys to

think through their case and to request only those documents that will assist them. An additional benefit of this change will be the elimination of the boxes of subpoenaed documents that line the hallways of the Division of Enforcement.

Third, the Task Force Report proposed an amendment that would require the Commission to return original documents within 30 days unless the director of the Division of Enforcement or the regional administrator for the region conducting the investigation has determined that there is a genuine need to retain the originals for a longer period. In this case, when the originals are no longer needed, they would be promptly returned.

Fourth, the Task Force Report would require the creation of a new position designated the “custodian of evidentiary materials.” The custodian would ensure the proper maintenance of documents produced during SEC investigations. Additionally, the proposed rule would require that, upon request, evidence produced during an investigation be returned once the investigation is concluded.

Finally, the Task Force Report would alter the Commission’s rules to permit an option that is not currently available—a challenge to an investigative subpoena at the administrative level. Under this proposal, if a witness and the staff fail to resolve their dispute, a member of the Commission or an administrative law judge would consider the motion and the staff recommendation on the papers without a hearing or oral argument. The Commission’s decision on such a motion would be a “preliminary, procedural, or intermediate agency action—subject to review [only] on the review of the final agency action.” If the recipient of the subpoena does not comply within five days of notice of the Commission’s adverse determina-

tion, enforcement proceedings may be initiated. This procedure is optional. A recipient may forgo this procedure and choose to challenge the subpoena in court *ab initio*.

The first four proposals described should be implemented. The fifth, while appealing in certain aspects, should not be adopted. A Commission investigation is similar to a grand jury subpoena. The SEC staff should not be forced to undergo an administrative proceeding before it can seek enforcement in the courts. The speed of a Commission investigation often means the difference between a successful and unsuccessful stock manipulation. To impede the investigation with administrative proceedings before allowing judicial enforcement is not warranted.

It is true that in the vast majority of cases under SEC investigation, the offense has been committed and the urgency of the situation does not demand expediency. However, this does not require the development of a device that would engender delay. Even after an offense has been committed, the public maintains an important interest in having enforcement matters presented in a timely fashion. Procedures that might delay the process should be rejected. The subject of an investigation will suffer no detriment by the Commission's refusal to adopt this proposal, since he still may contest a Commission subpoena in the courts.

The most appealing aspect of the proposal is that a party may challenge an SEC subpoena without the notoriety of a subpoena enforcement proceeding litigated in a federal district court. However, the concerns of a putative respondent can be alleviated without engrafting a new administrative procedure. There are viable, traditional procedures, such as confidentiality orders or bringing the proceeding against the respondent in the name of "John Doe." Challenges to grand jury subpoenas have traditionally been brought against parties using

the name “John Doe” to protect the confidentiality of the grand jury proceedings. Commission subpoena enforcement proceedings, like grand jury proceedings, are nonpublic. Although the SEC has not, to date, utilized “John Doe” proceedings, there is no reason why it could not.

Finally, a question often arises whether a motion to quash is proper when the staff seeks to question a witness twice—once during the investigation and again after the Commission has instituted an enforcement proceeding. In *SEC v. Saul*,^{xliii} the Court held that the SEC is not precluded from taking the deposition of individuals in the course of prosecuting a civil action filed after the conclusion of its administrative investigation despite the fact that the same individual had given testimony in the context of the administrative investigation that preceded suit. The Court reasoned that the SEC’s concern in the investigation is to determine whether to bring charges, while its concern after suit is trial preparation. This difference, in the absence of bad faith, is sufficient to allow the Commission to pursue its pretrial discovery rights despite its prior investigative testimony from the same witness.

XIII. Enjoining Investigation

An SEC investigation normally will not be enjoined by a federal court.^{xliv} However, if the investigation is so sweeping and unrelated to the Commission’s statutory power to investigate, a court may be justified in halting the investigation.^{xlv} The subpoena opponent must prove by a meaningful and factual showing that the Commission, not merely an investigator, had an improper purpose.^{xlvi} Naturally, state courts may not enjoin a Commission investigation on any ground because the federal government has not waived sovereign immunity, and the supremacy clause bars interference with federal administrative proceedings.^{xlvii}

Section 21(a) of the Securities Exchange Act and its accompanying regulations govern SEC investigations. Under § 21(a), the scope of review for abuse of discretion is limited. The Commission need only demonstrate some good faith basis for investigating since “Congress endowed the Commission with ‘broad powers’ to conduct investigations in support of its statutory mandate to protect the public interest through prompt and effective enforcement of the federal securities laws.”^{xlvi}

Unless the SEC is conducting an investigation that is clearly outside of its statutory mandate, the courts will be reluctant to interfere. Because the antifraud provisions and requirements of disclosure are so broad, and because the Commission may investigate to determine whether the securities laws have been violated or to ascertain if they are about to be violated, there will be few instances when a Commission investigation will be enjoined.

XIV. Subpoena Enforcement

The Commission enforces its subpoenas against non-complying witnesses by filing a summary proceeding under Fed. R. Civ. P. 81(a)(3). The Commission need not file a complaint, and, while the Federal Rules of Civil Procedure are generally applicable, their application may be limited if a literal reading would delay or unduly complicate the proceeding.^{xlix}

In order to obtain enforcement of a Commission subpoena, the staff must affirmatively make certain *prima facie* showings. Once this has been done, the burden to show that the Commission is acting in bad faith shifts to the party opposing enforcement.

XV. Commission’s Prima Facie Showing

In its application, the SEC need not show probable cause to obtain enforcement.¹ The showing required of the Commission has been defined by the courts in various ways. Most

courts have required that the SEC must meet the four-part test set forth in *United States v. Powell*,^{li} namely: (1) that the investigation is being conducted for a proper purpose; (2) that the information sought is relevant to that purpose; (3) that the information is not already within the Commission's possession; and (4) that the Commission's procedures have been followed.^{lii} Other courts have defined the showing by reference to the standards set forth in *United States v. Morton*, namely: that the inquiry (1) is not too indefinite; (2) is relevant to the investigation which the agency has authority to conduct; and (3) that all administrative prerequisites have been met.^{liii} Another court has referred to both the *Powell* and *Morton* standards simultaneously.^{liv} The Supreme Court has not addressed the precise formulation it will apply to determine the SEC's subpoena enforcement standards.^{lv}

The difference between the *Powell* and *Morton* standards is more semantical than substantive (except for *Powell's* requirement that the Commission not be in possession of the information),^{lvi} and thus the formulation applied will be of limited significance. Therefore, the Commission generally will make out its *prima facie* case with respect to *Powell's* or *Morton's* elements by submitting an affidavit^{lvii} attesting that the Commission has issued an order designating certain of its officers to investigate whether the statutes that it administers have been, are being, or are about to be violated; that one of those officers issued a subpoena for information relevant to the investigation described in the formal order; that the subpoena was properly served; and that the witness failed to comply.

When counsel examines the Commission's affidavit, submitted in support of a subpoena enforcement action, three issues require attention: (1) is the Commission authorized to conduct the investigation?,^{lviii} (2) is the information sought relevant?,^{lix} and (3) was the subpoena

properly issued and served?^{lx} The first two issues are addressed below, while the third issue, whether the subpoena was properly issued and served, is addressed above.

XVI. Lawfully Authorized

Normally, the Commission will have little difficulty demonstrating that its investigation is authorized and lawful. Production of the formal order of investigation setting forth the possible violations of the securities laws and implementing regulations normally will suffice. The suspected violations, listed in the formal order, will allow inquiry into a broad range of matters. As long as the investigation is within the Commission's statutory domain, the fact that the formal order does not specifically reference a matter being examined by the Commission will not form a basis for objection.^{lxi} Moreover, the scope of the Commission's statutory authority is an issue to be addressed initially by the SEC during the course of its investigation.^{lxii}

XVII. Relevancy

Relevancy means that the subpoenaed information or documents must be related to the Commission's investigative objectives,^{lxiii} *i.e.*, the investigation's specific purpose.^{lxiv} In formulating a test for relevancy in subpoena enforcement cases, the courts have held that an administrative subpoena will be enforced if the documents sought are not plainly immaterial or irrelevant to the investigation.^{lxv} While it has been argued that this test stands the burden of proof on its head, the courts consistently have rejected the argument and continue to formulate the test in this manner.^{lxvi}

The fact that a large volume of information has been requested is not controlling if the subpoenaed documents are relevant or material to the Commission's investigation. Indeed,

the complex and intricate nature of an SEC investigation often requires the production of large volumes of information.

Frequently a witness contends that the Commission's document request, while relevant, is overly broad and burdensome and requires some limitation. The Supreme Court has held that the Fourth Amendment requires an administrative subpoena to be "sufficiently limited in scope, relevant in purpose, and specific in directive so that compliance will not be unreasonably burdensome."^{lxvii} A witness making this argument bears the burden of showing that the subpoena is unreasonable. Indeed, if the agency's subpoena is authorized by law and the material sought is relevant, that burden is not easily met.^{lxviii} In order to meet this burden, the party opposing the subpoena will have to make the type of showing demonstrated in *Bank of America National Trust Savings Ass'n v. Douglas*.^{lxix} In that case, the court refused to enforce a subpoena that required the production in Washington, D.C. of records maintained in California covering a ten-year period of time where no evidence of their materiality was shown.

In *SEC v. Arthur Young & Co.*, the court tried to resolve the tension created by the volume of relevant records the Commission had subpoenaed and the burden placed upon the witness by requiring expense reimbursement as the price of enforcement.^{lxx} In *SEC v. Savage*, the Court indicated that a request for production of documents that could disrupt the business of the subpoenaed party would warrant a protective order. In that case, the Commission agreed to examine the records without removal from the business premises.^{lxxi} These remedies will not be ordered in all cases. Each case will depend upon its particular circumstances and the volume of documents required by the subpoena.^{lxxii}

XVIII. Defeating the *Prima Facie* Case—Lack of Good Faith

Regardless of whether the court applies *Powell's* or *Morton's* test, once the Commission has made out a *prima facie* case the burden shifts to the party contesting the subpoena to show that, due to the Commission's bad faith, enforcement would constitute an abuse of the court's process.^{lxxiii} Where the agency has made its *prima facie* showing, that burden is not easily discharged.^{lxxiv}

The respondent will normally attempt to show lack of good faith by disproving one of the elements of the Commission's *prima facie* case, or by demonstrating that judicial enforcement of the summons would otherwise constitute an abuse of the court's process.^{lxxv} The latter can be shown by evidence indicating that the subpoena was not issued in good faith, but rather to harass or to pressure the subject of the investigation for some other improper purpose. However, if the primary purpose of the subpoena is legitimate, an illegitimate secondary purpose will not preclude enforcement.^{lxxvi}

It has been held that the improper purpose must be that of the Commission rather than its investigators.^{lxxvii} However, it also has been held that a Commission subpoena will be denied enforcement where the SEC staff has initially gained access to information through fraud, deceit, or trickery and then attempts to use the power of the court to gather that information. In *SEC v. ESM Government Securities Inc.*,^{lxxviii} the court remanded a subpoena enforcement action to the district court to determine whether a Commission employee had knowingly or intentionally misled a broker-dealer to gain access to its files. The court indicated that if this question was answered in the affirmative, this would demonstrate the Commission's bad faith and warrant a refusal to enforce the subpoena.^{lxxix}

In *SEC v. Wheeling-Pittsburgh Steel Corp.*,^{lxxx} the Court indicated that judicial enforcement of a Commission subpoena may be denied where the Commission has acted in good faith but where the Court's process is abused. In that case, the investigation had been initiated by a powerful senator—ostensibly to protect local industry in his state at the expense of Wheeling-Pittsburgh. The Third Circuit determined that the Commission could not abdicate its responsibility to make impartial determinations on whether to investigate. It further held that if on remand the Commission's investigation was found to be dictated solely by external forces, the subpoena would not be enforced until the Commission reevaluated the case.^{lxxxi}

The *Wheeling-Pittsburgh* decision does not preclude all congressional involvement with the Commission, only involvement in its decisions on the merits. If the senator intervenes to accelerate disposition or enforcement of pertinent regulations, the agency's good faith in conducting the investigation is not at issue.^{lxxxii}

XIX. Discovery

There is no unqualified right to discovery in a subpoena enforcement case.^{lxxxiii} While the Federal Rules of Civil Procedure apply to a subpoena enforcement case, the court has the discretionary power under Fed. R. Civ. P. 81(a)(3) to limit discovery.^{lxxxiv} Indeed, discovery is the exception, not the rule, in summary proceedings.^{lxxxv}

If the party challenging the subpoena fails to refute the Commission's *prima facie showing* or to factually support an affirmative defense of bad faith, the Court will dispose of the proceedings on the papers before it. Conclusory allegations are insufficient to obtain discovery. The party challenging the subpoena must set forth specific facts to meet its burden.^{lxxxvi} The

party challenging the subpoena must show some evidence controverting the Commission's prima facie case or demonstrating its bad faith before discovery will be ordered.

When the witness comes forward with “meaningful evidence”^{lxxxvii} or “substantial allegations,”^{lxxxviii} limited discovery may be ordered.^{lxxxix} However, the court, in exercising its powers to supervise discovery, must strike a balance between allowing the witness access to evidence relevant to his defense and protecting the Commission from undue burden.^{xc} In striking that balance, full dress discovery will rarely be permitted and the court will normally limit discovery to the necessary minimum.^{xcii}

An example of an instance where a court will permit limited discovery is to afford a party an opportunity to demonstrate that a privilege against disclosure of confidential communications was properly preserved. For example, in *SEC v. Lavin*,^{xcii} the District of Columbia Circuit held that the district court erred in limiting discovery on the issue of confidentiality in a subpoena enforcement proceeding where the record was insufficiently developed to determine whether the marital communications privilege had been waived. In *Lavin*, the SEC sought production of taped recordings of several telephone conversations between spouses, the Lavins, in connection with an investigation into allegedly fraudulent sales practices in derivative securities. In challenging the enforcement of the subpoena, the Lavins claimed that because they had no knowledge that their conversations were being recorded, they had done nothing to compromise the confidentiality of their communications in a manner that would constitute a waiver of the marital communications privilege. Nevertheless, the district court denied the Lavins' request to depose and cross-examine witnesses relied upon by the SEC to support the allegation that Mr. Lavin knew his telephone was being recorded.

In reversing the district court's order enforcing the subpoena, the D.C. Circuit explained that the proper inquiry in determining whether the Lavins' conversations were protected under the marital communications privilege was whether special circumstances existed to require additional discovery, rather than whether the Commission acted in bad faith.^{xciii} Moreover, the court also noted that evidence related to the Lavins' knowledge of whether their conversations were being recorded was largely inconclusive. Because the Lavins' claim of privilege was not presented to the district court with appropriate deliberation and precision on the basis of a sufficiently developed record, the D.C. Circuit reasoned that the district court abused its discretion in denying the Lavins' discovery request.

Since discovery is limited even when authorized, counsel should frame its attack upon the subpoena as broadly as the available evidence will allow, such that any ordered discovery will have a broader scope. However, in framing the attack, the lawyer must bear in mind that mere protestations of innocence and claims of SEC bad faith will not result in a discovery order.

XX. Protective Orders

Once the SEC has commenced a subpoena enforcement action, the respondent may seek a protective order controlling access to the documents produced. Thus, during the investigations of Boeing and Lockheed for illegal conduct abroad, the court entered orders preventing the disclosure of subpoenaed documents or information, except to proper law enforcement agencies, until the Commission first afforded all interested parties the opportunity to seek a court order for relief.^{xciv}

In 1980, under the Freedom of Information Act, the Commission promulgated rules on the confidential bent of documents and information. These rules afford a subpoenaed witness the same measure of protection as was received by Lockheed and Boeing through a protective order.^{xcv} Under these rules, a party producing documents or information may request confidential treatment. Once confidential treatment is requested, the Commission must first notify the party who produced the information or documents before the Commission releases them, to afford an opportunity to obtain judicial relief.

While the types of protective orders issued in the *Lockheed* and *Boeing* cases are now covered by the Commission's regulations promulgated under the Freedom of Information Act, protective orders still have continuing vitality in other areas. Thus, the subpoenaed witness may seek a protective order controlling the time, place, and manner of production. Often the Commission will subpoena a mass of documentation and require its production in Washington, D.C. The respondent may determine that a protective order, requiring the Commission to inspect the records where located, is appropriate. In a proper case, the respondent may wish to control the order of production by requiring the Commission to first inspect one category of records before being allowed access to others.

XXI. Intervention

There is no absolute right to intervene in a Commission investigation.^{xcvi} Although the Federal Rules of Civil Procedure (including Rule 24(a)(2) dealing with intervention as of right) are generally applicable to subpoena enforcement actions by virtue of Rule 81(a)(3), the district courts may, by local rule or order, limit their applicability. As a result of the Supreme Court decision in *Donaldson v. United States*,^{xcvii} district courts have done so uniformly.

Because of the summary character of enforcement proceedings, in *Donaldson*, the Supreme Court held that a district court need not afford an intervenor an absolute right to participate under Rule 24(a)(2) in subpoena enforcement cases. Rather, the district court may allow intervention as a matter of discretion where the material sought is for an improper purpose, or to protect a claim of privilege.^{xcviii}

Intervention should not be afforded simply because the subpoenaed party maintains documents that relate or refer to the intervenor. Rather, a party should be allowed to enter a subpoena enforcement case only to guard a “significantly protectable interest.”^{xcix} Thus, in *SEC v. Dresser Industries*,^c the District of Columbia Circuit held that employees of a corporation might intervene in a subpoena enforcement action when specific questions of confidentiality and privilege affecting their interests were presented. Intervention in a subpoena enforcement case will depend upon the balancing of the equities involved;^{ci} that is, the Court will weigh the delay caused by intervention with the nature of the right the intervenor seeks to protect.

XXII. Parallel Proceedings

Often the Commission will conduct a parallel investigation into the same subject as a federal grand jury. Although there has been some controversy about such parallel investigations, courts have held that the existence of such parallel, ongoing, civil and criminal investigations does not prevent the enforcement of a Commission subpoena.

In the late 1970s, defense counsel routinely argued that simultaneous investigations resulted in the Commission’s process being used for criminal discovery,^{cii} thereby infringing the grand jury’s role in independently investigating allegations of criminal wrongdoing. With the Supreme Court’s decision in *United States v. LaSalle National Bank*,^{ciii} this argument developed

some force. In *LaSalle*, the Supreme Court held that the Internal Revenue Service's civil subpoena authority ceased, for all practical purposes, upon referral of the taxpayer's case to the Department of Justice. Defense attorneys contended, with *LaSalle* as their support, that a Commission investigation could not continue if a reference had been made to the Department of Justice or if access had been granted to the Commission's files. However, the controversy was short-lived. In *SEC v. Dresser Industries*,^{civ} the District of Columbia Circuit sitting en banc held that *LaSalle* did not apply to Commission investigations since the investigative provisions of the securities laws are far broader than the provisions of the Internal Revenue Code, as applied by the Supreme Court in *LaSalle*. Moreover, the Court held that there was no constitutional requirement that mandated a stay of civil proceedings pending the outcome of criminal proceedings.

The court in *Dresser Industries* also refused to adopt the panel's position that once the Department of Justice initiates a grand jury investigation the Commission may not provide it with the fruits of the Commission's civil discovery process. The D.C. Circuit held that where the Commission acts in good faith with a legitimate non-criminal purpose for its investigation, it may use the information gained in the investigation for criminal purposes as well.^{cv}

XXIII. Stays

The courts have often grappled with whether the existence of a criminal investigation or proceeding warrants a stay of an SEC investigation or an SEC civil action brought subsequent to a Commission investigation. The decision in *SEC v. Incendy*^{cvi} is typical of the attitude of the courts. A defendant broker-dealer moved to stay an SEC civil case seeking injunctive and equitable relief. The defendant argued that a stay was appropriate pending the resolution of a contemporaneous criminal indictment involving the same alleged violations of federal securities

laws. Because evidence presented in the SEC proceeding could be used against him in the criminal prosecution, the defendant asserted that mounting a vigorous defense in the civil case might reveal damaging information that would jeopardize the outcome of the criminal trial in violation of his Fifth Amendment privilege against self-incrimination. The *Incendy* court rejected this argument and held that “unless substantial prejudice to the rights of the parties is shown, simultaneous or successive prosecution of civil and criminal actions is permissible.”^{cvii} Relying in part on the rationale espoused in *Dresser*, the Court maintained that parallel criminal and civil proceedings may be necessary to safeguard the public interest, despite any disadvantage the defendant might suffer from his deliberate silence to avoid self-incrimination in a future criminal adjudication.^{cviii} While the Fifth Amendment does not bar adverse inferences from being drawn against a defendant who refrains from testifying in a civil case,^{ciix} it also does not prevent a defendant from exercising “his Fifth Amendment rights by not presenting evidence which would implicate him in [a contemporaneous] criminal proceeding[.]”^{cx} Thus, while the Fifth Amendment privilege is protected, its invocation comes with a price in a civil case.

This is not to say that a stay of an SEC civil case is never appropriate where there is a parallel criminal proceeding. Courts have postponed civil cases where the threat to the defendant of forgoing the civil action or facing criminal prosecution violated accepted notions of fundamental fairness.^{cxii} In determining the appropriateness of a stay in such cases, some courts employ a balancing test involving consideration of several factors, including the: (1) private interests of the plaintiffs in proceeding expeditiously with the civil action as balanced against the prejudice to the plaintiff resulting from the delay; (2) private interests of and the burden borne by the defendant; (3) convenience to the courts; (4) interests of persons not parties to the civil litigation; and (5) the public interest.^{cxiii} Moreover, other means short of a complete stay of

proceedings are at the courts' disposal to accommodate the variety of interests and circumstances presented in each case. For example, courts may delay discovery and depositions,^{cxiii} limit the scope of witness examinations,^{cxiv} and enter protective orders to curtail unwarranted disclosure of potentially incriminating discovery to the government.^{cxv} Furthermore, courts are free to fashion discovery schedules tailored to protect the interests of all parties.^{cxvi}

XXIV. Collateral Estoppel

Collateral estoppel, also known as issue preclusion, is a legal doctrine that bars a party or his privy from relitigating an identical issue that was decided on the merits in an earlier proceeding.^{cxvii} It applies only if the following criteria are satisfied: (1) the identical issue raised in the present case must have been raised and actually litigated in the prior proceeding; (2) determination of the issue must have been legally necessary to the outcome of the prior proceeding; (3) the prior proceeding must have resulted in a final judgment on the merits; and (4) the party against whom collateral estoppel is sought must have been afforded a full and fair opportunity to litigate the issue in the prior proceeding.^{cxviii} Collateral estoppel aims at “reducing the burdens associated with revisiting an issue already decided,”^{cxix} and reflects the view that even “the occasional encapsulation of a wrong result is a price worth paying to promote the worthy goals of ending disputes and avoiding repetitive litigation.”^{cxx}

Collateral estoppel may affect profoundly the relationship between parallel civil and criminal proceedings by precluding a defendant in a civil action from denying allegations because of prior criminal convictions based on factually related charges, regardless of whether the SEC was a party to the prior criminal action.^{cxxi} In *SEC v. Smith*,^{cxxii} the Commission appealed preliminary injunctions entered against it, enjoining the agency from prosecuting a civil enforcement action pending the court's determination of whether the Commission had illegally

obtained a tape recording, which directly implicated the defendant in insider trading. While the appeal in the civil action was pending, the defendant was indicted for insider trading in another federal district court. He then moved that court to suppress evidence in the criminal action that had been derived from the tape. The court denied the motion, finding that the government's "evidence of insider trading was derived not from the tape, but from [its] independent investigation of the facts."^{cxiii} The defendant ultimately was convicted on the basis of that evidence.

In vacating the injunctions entered in the civil enforcement action, the United States Court of Appeals for the Sixth Circuit reasoned that the defendant was without basis in asserting that he would be irreparably injured absent the injunctions barring the SEC's use of the tape because neither it nor evidence derived from it was essential to the Commission's case. The court explained that, in light of the defendant's prior criminal conviction which was based on evidence gleaned from sources other than the tape, "[i]n order to prevail in the civil action, the SEC now needs only to move for summary judgment on the basis of the collateral estoppel effect of that conviction."^{cxiv}

As the United States Court of Appeals for the Second Circuit recognized in *SEC v. Monarch Funding Corp.*,^{cxv} however, there are some situations "that so undermine confidence in the validity of an original determination as to render application of the doctrine impermissibly 'unfair' to a defendant."^{cxvi} There, the Second Circuit concluded that there is a rebuttable presumption against precluding relitigation in a civil action on the basis of factual findings made in a prior criminal sentencing proceeding.

In support of its decision, the Second Circuit cited several reasons why giving sentencing findings preclusive effect in a subsequent civil action generally is unfair: (1) a plenary civil trial affords a defendant procedural opportunities that are unavailable at sentencing and that could command a different result, such as greater access to discovery and evidentiary protections under the Federal Rules of Evidence; (2) a defendant's incentive to prosecute vigorously a sentencing finding is frequently less intense, and riskier, than it would be for a full blown civil trial; and (3) extending collateral estoppel to the sentencing context likely would increase, rather than reduce, total litigation by unnecessarily encouraging more exhaustive and complex sentencing litigation over matters of only tangential significance to the criminal case.

On the other hand, the court noted that although “extending collateral estoppel effect to sentencing findings may, in a given case, threaten fairness and/or judicial efficiency, these factors do not justify a blanket prohibition [of the doctrine].”^{»cxxxvii} Rather, it concluded that “[s]o long as the threat to fairness and/or efficiency has been minimized, we see no reason to entirely foreclose application of [collateral estoppel].”^{»cxxxviii}

The Second Circuit in *Monarch Funding Corp.* established the standard for lower courts to apply in determining whether to give sentencing findings collateral estoppel effect in a subsequent civil action. Specifically, it determined that “precluding relitigation on the basis of such findings should be presumed improper,” and cautioned that collateral estoppel “should be applied only in those circumstances where it is clearly fair and efficient to do so.”^{»cxxxix} The court emphasized that a district court first should consider whether applying the doctrine to sentencing findings would promote judicial efficiency and, if it would not, the court “should feel free to deny preclusion for that reason alone.”^{»cxxx}

XXV. Fifth Amendment Privilege Against Self-Incrimination

The Fifth Amendment to the United States Constitution accords an individual the privilege against self-incrimination when the government compels the presentation or production of incriminating evidence that is testimonial in nature.^{cxxxix} The right applies not only in civil, criminal, and discovery proceedings, but also privileges an individual to refrain from responding to official questions posed in any proceeding, formal or informal, in which the answers might prove incriminating in subsequent criminal proceedings.^{cxxxii} Accordingly, the Fifth Amendment privilege against self-incrimination applies in SEC investigations.

However, the Fifth Amendment only protects individuals.^{cxxxiii} The privilege is not available to corporations^{cxxxiv} or custodians of corporate records,^{cxxxv} the government,^{cxxxvi} or other collective entities including labor unions,^{cxxxvii} partnerships,^{cxxxviii} and joint-ventures. Moreover, the privilege may be waived. While a waiver in one proceeding is not a waiver in subsequent proceedings, nothing prohibits the trier of fact in the subsequent proceeding from considering an incriminating statement.^{cxxxix}

Unlike in criminal cases,^{cxli} invocation of the Fifth Amendment privilege in a civil proceeding does not bar adverse inferences drawn against a party seeking its protection. In *Baxter v. Palmigiano*,^{cxli} the Supreme Court held that an inmate facing a prison disciplinary hearing, who was not only advised of his right to remain silent, but also forewarned that his refusal to testify in response to inculpatory, probative evidence could be held against him, suffered no deprivation of his Fifth Amendment right. The Court observed that the practice of weighing a party's refusal to testify in a prison disciplinary adjudication did "not smack of an invalid attempt by the State to compel testimony without granting immunity or to penalize the exercise of the privilege."^{cxlii} The Court emphasized that: (1) no criminal proceedings were

pending against the defendant; (2) the State made no effort to make evidentiary use of the inmate's silence in a later criminal proceeding; and (3) the State did not insist or request that the defendant waive his Fifth Amendment privilege. Moreover, the Court also noted that the inmate's decision to refrain from testifying was not dispositive in determining the outcome of the proceeding but, rather, was accorded the same evidentiary weight as other facts relevant to the case.^{cxliii} Thus, because of the Court's holding in *Baxter*, defendants in civil cases confronting a parallel criminal prosecution often face a Catch-22: remain silent in the civil proceeding and suffer the consequences of the adverse inference, or testify and risk the detrimental impact that may result from incriminating admissions.^{cxliv}

As the above indicates, a witness testifying during an SEC investigation may clearly claim the Fifth Amendment. However, the staff may argue to the Commission that an adverse influence should be drawn against that witness in determining whether to bring an SEC civil enforcement proceeding against him. Is an SEC investigation a civil proceeding in which an adverse influence can be drawn or a criminal proceeding? The SEC Supplemental Information form attached hereto as an appendix advises that the witness's testimony can be used in any subsequent civil or criminal proceeding.

In *SEC v. Futrex, Inc.*,^{cxlv} Chief Judge Norma Holloway Johnson of the United States District Court for the District of Columbia held that the Commission staff may draw adverse inferences from a party's refusal to testify in response to questions posed in an agency investigation in determining whether to level civil enforcement charges. Relying on *Baxter* without explanation, the court simply stated that "even if the [SEC] staff did argue that the Commission should draw an adverse [inference] from the [defendant's] silence, such an argument would not have violated [the defendant's] constitutional rights."^{cxlvi}

On the one hand, several arguments underscore the *Futrex* holding, and yet were never addressed in the court's opinion. First, the court failed to consider the applicability of adverse inferences in an SEC investigation, a non-civil proceeding. In *Baxter*, the Supreme Court stated that "the Fifth Amendment does not forbid adverse inferences against parties to civil actions when they refuse to testify in response to probative evidence offered against them."^{cxlvii} Yet, an administrative investigation is distinct and separate from any civil action that may eventually flow from it.^{cxlviii} Thus, it is uncertain why the *Futrex* court concluded that an adverse inference was permissible in the context of an SEC investigation, a non-civil proceeding.

Second, the *Baxter* Court observed that adverse inferences derived from an inmate's silence in a prison disciplinary proceeding are constitutionally permissible, in part, because such proceedings "involve the correctional process and important state interests other than conviction for a crime."^{cxlix} The Court carefully distinguished the remedial and corrective purposes that underlie prison disciplinary hearings from the uniquely adversarial aims of criminal proceedings, noting that the distinction justifies even a denial of appointed counsel for inmates facing disciplinary adjudication. However, this distinction is inapplicable in the context of SEC investigations that differ from prison disciplinary proceedings in one glaring respect: unlike the prison inmate, a party who invokes the Fifth Amendment privilege in response to questions posed in an SEC investigation may be subject to criminal prosecution. Because the corrective and other state purposes inherently a part of prison disciplinary proceedings attach only after a criminal conviction, interests other than conviction that justify treating civil cases differently with respect to adverse inferences are irrelevant in the context of an SEC investigation that typically precedes a criminal prosecution. Regrettably, the *Futrex* court offered no explanation for the apparent discrepancy.

In contrast, other arguments support the proposition that an adverse inference drawn in response to a party's refusal to testify in an SEC investigation is not inconsistent with Fifth Amendment commandments. In the first place, while the *Baxter* Court held that adverse inferences may be drawn in civil cases on account of a party's silence, nothing contained in the Court's opinion suggests that civil cases are the only setting where such action is permissible. Second, the *Baxter* Court reasoned that because the stakes in criminal cases are higher than in civil cases, the Fifth Amendment prohibits a judge or prosecutor from instructing a jury that a defendant's silence may be regarded as indicative of guilt.^{cl} Thus, because the interests at stake in a civil action exceed those implicated in an SEC investigation, *a fortiori* interests at stake in an SEC investigation do not rise to the level at stake in criminal proceedings that is sufficient to require the preclusion of adverse inferences. The *Futrex* court was silent with respect to this contention as well.

XXVI. Subsequent Withdrawal of the Fifth Amendment Privilege

A question frequently arises whether a defendant who has claimed the Fifth Amendment during the course of an SEC investigation and during the course of depositions in a subsequent civil enforcement proceeding may withdraw when faced with a motion for summary judgement or the prior invocations of the Fifth Amendment privilege against self-incrimination at trial. This raises a difficult legal issue, because while a litigant's constitutional right to avoid self-incrimination must be respected, the rights of other litigants are entitled to consideration as well. The assertion of the Fifth Amendment privilege deprives an opposing litigant of potentially vital information in determining the outcome of a civil action. Thus, the potential for abuse of the privilege is significant.

The United States Court of Appeals for the Second Circuit in *United States v. Certain Real Property & Premises Known as 4003-4005 5th Avenue*^{cli} addressed the appropriate considerations that should be accorded competing interests at stake in cases where a party seeks to withdraw the privilege. In *4003-4005 5th Avenue*, a defendant in a civil forfeiture action attempted to withdraw the prior invocation of his Fifth Amendment privilege to defend against the government’s motion for summary judgment. Acknowledging the defendant’s unenviable dilemma, the court instructed that upon a timely motion by a claimant to waive the privilege, “the court should explore all possible measures in order to select that means which strikes a fair balance and accommodates both parties.”^{clii} Moreover, the court also noted that consideration should be given “to the nature of the proceeding, how and when the privilege was invoked, and the potential for harm or prejudice to opposing parties.”^{cliii} The appropriate accommodations that a trial court may devise “necessarily depend[] on the precise facts and circumstances of each case.”^{cliv}

Generally, however, courts take a liberal view toward requests to withdraw the privilege that facilitate “adjudication based on consideration of all the material facts”^{clv} In the absence of prejudice or harm suffered by an opposing party, courts are inclined to allow withdrawal or fashion reasonably lenient remedies. For example, in *SEC v. Graystone Nash, Inc.*,^{clvi} the United States Court of Appeals for the Third Circuit reversed a district court grant of summary judgment against several defendant broker-dealers. The defendants initially asserted their Fifth Amendment privilege during discovery and later sought to withdraw the privilege to contest a motion for summary judgment. In response to the defendants’ attempts to jettison the privilege, the district court barred them from offering any evidence in opposition to the government’s motion for summary judgment. The Third Circuit noted that the district court

erred in failing to “carefully balance the interests of the party claiming protection against self-incrimination and the adversary’s entitlement to equitable treatment.”^{clvii} Specifically, the court noted that the district court failed to consider: (1) the significance of the defendants’ pro se appearance; (2) the continued vitality of the privilege in light of the defendants’ prior sworn testimony at an earlier proceeding and affidavits concerning matters which the defendants refused to discuss at their depositions; (3) the absence of any evidence indicating that the SEC was prejudiced by the defendants’ belated attempt to rescind the privilege; and (4) the lack of evidence to support the contention that the SEC would have been unable to present a formidable case if the defendants were permitted to testify.^{clviii} While the imposition of appropriate remedial measures is typically left to the discretion of the trial court, the *Graystone Nash* court explained that “[w]hen significant factors are not weighed in making that determination . . . we must remand so that a proper evaluation may be reached.”^{clix}

On the other hand, when parties employ the Fifth Amendment privilege as a device to abuse, manipulate, or obstruct the litigation process, courts have broad discretion to fashion remedies or impose appropriate sanctions.^{clx} Specifically, courts are authorized, especially in cases involving “eleventh hour” requests to withdraw, to bar a litigant from testifying concerning matters which he previously concealed from discovery through the improvident use of the privilege. For example, in *SEC v. Softpoint, Inc.*,^{clxi} the court barred the later testimony of a defendant who had previously invoked his privilege against self-incrimination not to shield himself from the compulsion to provide inculpatory testimony, but rather to force a change of venue for a pre-trial deposition. The *Softpoint* court explained that a witness may not invoke the Fifth Amendment privilege to frustrate the SEC’s investigation and later waive the privilege to avoid the undesirable consequences of the earlier refusal to testify.

XXVII. Other Privileges

The federal common law also recognizes the confidential, marital communications privilege that protects private communications between spouses conducted under the auspices and confidence of a marital relationship.^{clxii} The justification underlying this privilege is that “the immunity given to communications between husband and wife is the protection of marital confidences . . . so essential to the preservation of the marriage relationship as to outweigh the disadvantages to the administration of the justice which the privilege entails.”^{clxiii} To invoke the confidential communications privilege, the party claiming its protection must demonstrate that (1) there was a communication,^{clxiv} (2) there was a valid marriage at the time of the communication,^{clxv} (3) the communication was made within the confidence and privacy of the marital relationship,^{clxvi} and (4) the privilege was not waived.^{clxvii}

In *SEC v. Lavin*,^{clxviii} the United States Court of Appeals for the District of Columbia Circuit considered the applicability of the confidential marital communications privilege in the context of SEC investigations. In *Lavin*, a derivatives trader appealed a district court order enforcing a subpoena duces tecum for seven taped telephone conversations between the trader and his wife. These conversations were obtained by a taping system that recorded calls on the trader’s private office telephone line. However, the trader claimed no knowledge of the recording system, and upon learning of its existence, ordered it removed.^{clxix} What makes the *Lavin* decision unique is that the trader’s refusal to comply with an SEC subpoena was based upon the marital privilege with respect to communications memorialized on tapes which belonged to the trader’s employer. Thus, the trader maintained no control over the preservation or disclosure of the taped conversations. The *Lavin* court concluded that in instances where involuntary disclosure by third-parties threatens the protection of marital communications, the

privilege is preserved so long as the privilege holder acts reasonably in attempting to preserve it.^{clxx}

XXVIII. Inadvertent Disclosure

A defendant in an SEC investigation or a civil enforcement action must exercise due care to prevent the inadvertent disclosure of privileged materials. Although the mistaken production of privileged documents will not always constitute a waiver of the privilege, it may if “the producing party or its counsel was so careless as to suggest that it was not concerned with the protection of the asserted privilege.”^{clxxi} In determining whether an unintended production of privileged materials constitutes a waiver, courts consider: (1) the reasonableness of the measures taken to safeguard against inadvertent disclosure; (2) the time taken to correct the error; (3) the scope of the discovery and the extent of the disclosure; and (4) overarching issues of fairness.^{clxxii}

In *SEC v. Cassano*^{clxxiii} the court determined that the Commission’s inadvertent production of a privileged document resulted in a waiver where counsel had acted “so careless[ly] as to surrender any claim that it ha[d] taken reasonable steps to ensure confidentiality.”^{clxxiv} There, the SEC mistakenly produced for inspection by defense counsel a privileged, internal Staff memorandum outlining in detail the strengths and weaknesses of its case against the defendants. Inexplicably, the document had been neither separated from those intended for production, nor stamped “privileged” or “confidential,” as was commonly done to identify protected materials. Also, when defense counsel discovered the memorandum and asked that it be copied immediately, despite the prearrangement that all documents of interest to the defense would be set aside for later copying, the SEC attorney in charge granted the request without inspecting the document, either to ensure that it was non-privileged or to ascertain why it was so significant that defense counsel wanted only that document— one document out of 50 or

52 boxes of materials provided for inspection— turned over immediately. The court concluded that “[a]ny other precautions that were taken [by the SEC], and there certainly were some, fade into insignificance in the face of such carelessness.”^{clxxv}

In addition, the *Cassano* court reasoned that, although the mistaken disclosure of one or a few privileged documents in an otherwise voluminous production may not result in a waiver, the Commission was not entitled to such leniency because the specific document had been brought to its counsel’s attention, and counsel then made “[a] deliberate decision . . . to produce it without looking at it.”^{clxxvi} The court also noted that there was no excuse for the SEC attorney’s “waiting 12 days to find out what the document was,”^{clxxvii} and concluded that there was no reason, in light of overarching concerns of fairness, why the Commission’s carelessness should be disregarded.^{clxxviii}

XXIX. Venue

The Commission has a wide range of venue options when determining where it will commence a subpoena enforcement action. By statute, such an action may be commenced “within the jurisdiction of which such investigation or proceeding is carried on, or where such person resides or carries on business.”^{clxxix} Therefore, Commission attorneys would be well advised to research the law of each jurisdiction before choosing a venue. For example, the Commission might wish to avoid the Third Circuit which has adopted a rather stringent standard for good faith.^{clxxx}

The Commission’s venue choices are not unlimited, and the court will not permit the SEC to enforce a subpoena in a district that has no relationship to the focus of the agency’s investigation. In *SEC v. Financial Institutions Assurance Corp.*,^{clxxxi} the Commission was

investigating a company engaged in business only in North Carolina, and all documents sought were maintained there. Enforcement of the subpoena was sought in Atlanta solely on the ground that the Commission employees, who were conducting the investigation, were assigned to the Atlanta regional office, and because all decisions were made by that office with respect to the investigation. The court found those facts to be inadequate to sustain venue, holding that the forum must have some connection with the subject matter of the investigation or with the information sought.

XXX. Contempt

When a court orders a witness to comply with a Commission subpoena, any failure to obey that order will be punished as a contempt of court.^{clxxxii} The court may punish disobedience by subjecting the contemnor to civil or criminal contempt or both. Criminal contempt is imposed to punish the witness's disobedience while civil contempt coerces compliance.^{clxxxiii}

The court may punish a corporate officer for contempt where he appears on behalf of a corporation that has been ordered to produce documents, and where he fails to surrender subpoenaed records that are in existence and within his control.^{clxxxiv}

There have been relatively few contempt proceedings brought by the SEC against recalcitrant witnesses. This is probably because an order requiring compliance with a Commission subpoena is appealable.^{clxxxv} Those contempt proceedings that have been brought are mainly civil, presumably because the Commission is more interested in obtaining information than in bogging itself down in the procedural requirements surrounding criminal contempt. The defenses to a civil contempt action are limited. A contempt order will issue

unless the witness lacks the capacity to comply.^{clxxxvi} The burden of proving impossibility of compliance is on the contemnor.^{clxxxvii}

XXXI. Section 21©

In addition to initiating subpoena enforcement actions and contempt proceedings against recalcitrant witnesses, the Commission can also invoke § 21© of the Securities Exchange Act of 1934. That section provides that a witness who, without just cause, fails to appear or produce books and records when subpoenaed by the Commission is guilty of a misdemeanor punishable by a fine of \$ 1,000 or imprisonment of not more than one year.^{clxxxviii} Although this section is rarely utilized,^{clxxxix} it exists and can be dragged out of the closet by the SEC when faced with a refusal to appear or produce without any basis.^{cxc}

XXXII. Wells Submission

At the conclusion of an investigation, the SEC staff will determine whether to recommend an enforcement proceeding. If the staff believes that the securities laws have been violated, it can recommend the institution of an administrative proceeding looking to the imposition of remedial sanctions, initiation of injunctive proceedings in the courts, and, in the case of a willful violation, the reference of the matter to the Department of Justice for criminal prosecution. Additionally, the staff may refer the matter to other domestic and foreign governmental authorities and self-regulatory organizations such as stock exchanges or the National Association of Securities Dealers.^{cxc}

If the staff concludes that such proceedings are unwarranted, however, it may, in its discretion, advise the parties that the investigation has been terminated. Such advice, however, does not indicate that the party has been exonerated or that no action may ultimately result.^{cxcii}

When the staff determines that it will recommend an enforcement proceeding, it may advise the persons against whom the action will be recommended of its intention and afford them an opportunity to make a written Submission to the Commission setting forth their position.^{cxci} The objective of the Submission is to place before the Commission, prior to the authorization of an enforcement proceeding, the position of the staff and of the adverse party concerning the facts and circumstances that form the basis for the staff recommendation. This Submission is commonly called a “Wells Submission.”

The purpose of a “Wells Submission” is not to resolve factual disputes between the staff and a prospective respondent. Rather, the Submissions are most useful in connection with questions of policy and, on occasion, questions of law bearing upon the question of whether a proceeding should be initiated. They also illuminate considerations relevant to a particular prospective defendant or respondent, which factors otherwise may not be brought to the Commission’s attention.^{cxci} These Submissions should be forwarded to the appropriate division director or regional administrator, with a copy to the SEC staff members conducting the investigation. The “Wells Submission” will then be forwarded to the Commission along with the staff’s memorandum. The right to make a “Wells Submission” is not constitutionally protected.^{cxci} Furthermore, the staff’s failure to allow a “Wells Submission” does not warrant dismissal of the Commission’s action.^{cxci} Indeed, as the Commission’s own rules note, the staff may, in “its discretion,” advise the putative defendants of the charges it intends to recommend.^{cxci}

The Task Force Report has proposed an amendment to the Rules Relating to Investigations that would make the “Wells Submission” more meaningful. Some of the Commission’s staff are reluctant to define fully the nature of the charges and their factual basis.

The proposed rule would require the staff to notify a prospective defendant of the charges to be recommended, the role of the proposed defendant, and the factual and legal basis for the charges. Finally, the Task Force has recommended that 30 days should be presumed as reasonable time to prepare the “Wells Submission.”

XXXIII. Admissibility Of Wells Submissions

Disclosure! Disclosure! Disclosure! Disclosure is the word that the Commission lives by. It prides itself on being a full-disclosure agency. Its philosophy is that the public markets in this country thrive on information. In order for the free-market system to operate properly, all material information must be made available to investors. However, that same full disclosure agency has a system of secret polices that it applies to those with whom it deals. These secret policies are nowhere written down, but are trotted out of the staff’s bag of tricks whenever they are met with cogent and legitimate arguments made by defense counsel.

For example, from time to time, the staff claims that counsel for a witness may only obtain a copy of the Commission’s formal order of investigation if he agrees not to show it to anyone but the client. Of course, there is no such requirement in the Commission’s Rules Relating to Investigations.^{excviii} The staff’s interpretation is merely a policy gloss they have appended to the rule. But, the most notorious of these secret policies is the claim that the Division of Enforcement will not accept a Wells Submission that attempts to place conditions on the Submission or to limit its admissibility in any proceeding. I recently ran across this unwritten policy when I made a Wells Submission, which contained a footnote invoking Federal Rule of Evidence 408. That Rule states, in essence, that statements made in compromise negotiations are not admissible. Within a day of submitting the Wells Submission, I received a call from a staff attorney at the Commission demanding that I delete the footnote containing the

Rule 408 language. He argued that it was the policy of the Division of Enforcement not to accept such a Wells Submission, and if I did not agree to delete the footnote, the staff would reject my Submission and return it to me. I asked the staff attorney where this so-called “policy” was set forth in writing. He was unable to tell me where either the Commission or the Division of Enforcement had set forth that policy, but persisted in his threat to return the Wells Submission if the offending footnote was not removed. The staff attorney insisted that the Trial Unit of the Division of Enforcement believes it is imperative that Wells Submissions be available for admission into evidence against the submitter in any subsequent proceedings. I explained that while I had served in the Trial Unit some 16 years before, I never had heard of this “policy.”

I added that, unlike many of my brethren in the securities bar, I believe that, except in unusual cases, Wells Submissions are at best a waste of time and at worst a road map of the defense’s theory of the case. Indeed, when the Commission issued its release advising the public of its Wells process, it stated that disputed issues of fact would not normally be resolved by the Commission during the Wells process. Rather, the submissions are most useful in connection with questions of policy and occasionally concerning questions of law bearing upon whether a proceeding should be initiated.^{cxciix} Because so few cases involve questions of policy or pure questions of law, it has been my practice for over ten years not to make Wells Submissions.

I have been criticized by the staff for this practice. In the late 1980s, I litigated a case called *SEC v. Amster & Co.*,^{cc} in which I obtained summary judgment against the Commission. After this victory, the staff chastised me for not having made a Wells Submission pointing out the case’s deficiencies. The staff contended that if I had only made a Wells Submission, the staff would have realized that it had no case and forgone prosecution. Anyone who has sat across the table from an SEC staff attorney and witnessed the flames spewing from his or her nostrils and

the smoke billowing out of his or her ears while discussing potential charges against your client knows that the chances of a Wells Submission convincing the staff it is wrong are somewhere between little and none. Despite the staff's admonishment, over the years I have remained steadfast in my belief that Wells Submissions are ineffective and I have continued not to submit them.

Recently, however, I was faced with an investigation in which the Staff advised me that it would recommend an enforcement action, a recommendation which I believed lacked any basis in fact or law. Hoping that an objective observer would read my Submission—perhaps even a Commissioner—I decided to abandon my practice and make a Wells Submission. When I did, I included a footnote invoking Federal Rule of Evidence 408, stating that my Submission was made in the spirit of compromise and, therefore, should not be deemed to be admissible evidence in any subsequent proceeding. Thereafter, I received the telephone call from the staff demanding that the offending language be taken out.

In order to get the Commission to review my Wells Submission, I agreed to remove the offending language, but simultaneously filed a Freedom of Information Act request under 5 U.S.C. § 552 asking for a copy of the policy of the Commission or the Division of Enforcement not to accept a Wells Submission that places conditions on the Submission or limits its admissibility in any proceeding. To my astonishment, two weeks later I received a letter back from the Commission (a copy of which is attached hereto) stating that after consultation among its Divisions, the Commission could find no materials relating to *any* such policy. I conclude from this that, in fact, there is no policy of either the Commission or the Division of Enforcement not to accept a Wells Submission with such language, and that the staff's refusal to accept a Wells Submission with that language is merely a part of what SEC enforcement attorneys refer

to as SEC “lore.” While it is gratifying to one’s ego to be part of the “cognoscenti” who are aware of this secret body of “lore,” in a democracy, the existence of secret government polices is inappropriate. Moreover, such secret polices are a direct violation of the Administrative Procedures Act. Indeed, Congress enacted the Administrative Procedures Act because it was concerned with the dilemma in which the public finds itself when forced to litigate with agencies on the basis of secret law or incomplete information.

Under the Administrative Procedures Act, agencies are required to publish in the Federal Register substantive rules of general applicability and statements of general policy or interpretation formulated and adopted by the agency.^{ccci} The Commission’s own rules mimic those of the statute.^{ccii} The Administrative Procedures Act further provides that statements of policy or interpretations that have been adopted by an agency and are not published in the Federal Register shall be available to the public for inspection and copying.^{cciii}

In either case, enforcement “lore” violates the Administrative Procedures Act. If the staff’s refusal to accept a Wells Submission containing Rule 408 language is a general policy, it is ineffective for lack of publication in the Federal Register.^{cciv} A statement of general policy is defined as “statements issued by an agency to advise the public prospectively of the matter in which the agency proposes to exercise a discretionary power.”^{ccv} If the staff’s position is only a policy or interpretation of its Rules Relating to Investigations^{ccvi} and not a statement of general policy, it is ineffective because it is not available for public inspection and copying.^{ccvii} In any event, it is clear that the Administrative Procedures Act prevents *ad hoc* interpretation of the rules by the staff of the Division of Enforcement.

Moreover, this alleged policy of the Commission is at odds with the Federal Rules of Evidence, which, of course, apply to any enforcement proceeding brought by the Commission. It is also at odds with the Commission's own written and promulgated procedures with respect to Wells Submissions. For example, § 202.5© specifically provides that a person may on his own initiative submit a written statement to the Commission and "[i]n the event a recommendation for the commencement of an enforcement proceeding is presented by the staff, any Submissions by interested persons will be forwarded to the Commission in conjunction with the staff memorandum."^{ccviii} Thus, the Commission's own rules state that any Submission will be forwarded to the Commission. It says nothing about forwarding only those Submissions that do not contain language invoking Federal Rule of Evidence 408. Indeed, the Commission's own announced policy encourages Wells Submissions and the settlement of cases in accordance with Rule 408. Thus, when promulgating § 202.5©, the Commission specifically stated: "It is hoped that this release will be useful in encouraging interested persons to make their views known to the Commission"^{ccix}

Moreover, this alleged policy of the Commission is in direct conflict with the opinions of at least three of the Commission's administrative law judges who have expressed the impropriety of using Wells Submissions as evidence in administrative proceedings. Thus, in the case of *In re Allied Stores Corp.*,^{ccx} the administrative law judge stated:

It is clear . . . that the Commission's intention [in promulgating the rule that invites interested parties to make Wells Submissions] was to encourage Submissions in the interest of resolving or settling the basic question whether enforcement action should be instituted. In that light, a Wells Submission should be treated as a document entitled to the protection accorded documents used in connection with settlement negotiations.

The administrative law judge rejected as unacceptably narrow the views expressed by the Division of Enforcement that the Wells Submission procedure is to inform the Commission and not to encourage settlements. It concluded that permitting Wells Submissions to be introduced into evidence would be a deterring factor inconsistent with the encouragement that the Commission has given to the making of those statements.

In the case of *In re Boston Co. Institutional Investors, Inc.*,^{ccxi} Administrative Law Judge Markun stated:

Wells committee submissions, in the context in which they are made, may take on certain aspects of “plea bargaining” or “settlement” discussions. It is unknown for the Commission under current practice to institute a proceeding and set forth the terms of settlement in the same order. Where that is involved, Rules 408 and 410 of the Federal Rules of Evidence, 88 Stat. 1927, excluding from evidence offers to settle or to plead guilty, respectively, are of interest

Similarly, in *In re Flagship Securities, Inc.*,^{ccxii} Chief Administrative Law Judge Murray declined to review Wells Submissions that the Division of Enforcement attempted to submit as evidence.

Thus, it is absolutely clear that the current state of the law impugns the validity of any purported policy of the Division of Enforcement prohibiting Wells Submissions from containing Rule 408 language. It is no wonder in light of this clear record that the Division of Enforcement has not set forth its policy in writing, but instead has attempted to disguise as SEC “lore” what are the facts. It is time for the securities bar to advise the new Director of the Division of Enforcement, Richard Walker, that the misuse of unwritten, *ad hoc* policies adopted by the staff

is inappropriate.^{ccxiii} We are entitled as American citizens to be treated fairly and to not be subjected to a regime of secret unwritten policies.^{ccxiv}

XXXIV. Statute of Limitations

While the SEC's authority to conduct investigations is nearly unrestricted, its ability to impose disciplinary sanctions is not. In *Johnson v. SEC*,^{ccxv} the District of Columbia Circuit held that 28 U.S.C. § 2462, the federal "catch-all" five-year statute of limitations,^{ccxvi} applies to SEC disciplinary proceedings instituted under § 15(b) of the Securities and Exchange Act of 1934. *Johnson* involved a securities industry supervisor who failed to detect and deter the thievery of a subordinate employee. The Court concluded that the SEC's sanctions—censure and six-month suspension—constituted a "penalty"^{ccxvii} within the meaning of § 2462.^{ccxviii} The court maintained that the character of the sanctions was more punitive than remedial because they (1) limited the defendant's ability to earn a living; (2) ruined any hope of professional advancement; (3) were not predicated upon the defendant's existing inability to properly supervise subordinates or any risk to the public posed by her continued employment, but rather upon the defendant's prior failure to discharge her duties; and (4) were not calculated to return the stolen funds to their rightful owners. An apparent consequence of the *Johnson* decision is that the SEC will ultimately have to initiate and complete investigations more quickly to avoid running afoul of the time limitations under § 2462.^{ccxix}

XXXV. The Power of the Commission

In the past few years, the SEC's power to conduct investigations and subsequent enforcement litigation has come under challenge.

In *SEC v. Blinder, Robinson & Co.*,^{ccxx} the Commission sought enforcement of an administration subpoena *duces tecum* against Blinder, Robinson & Co. (“BRC”), a nationwide broker-dealer. BRC argued that under Article 2, § 3 of the U.S. Constitution, only the President of the United States may exercise the executive function of enforcing the laws. Therefore, according to BRC, the enforcement provisions of the Securities Exchange Act of 1934^{ccxxi} violated the constitutional separation of powers. BRC argued that because SEC commissioners can be removed only for cause, the President lacks sufficient control over the Commission and as such cannot discharge his constitutional obligation to ensure that the laws are faithfully executed. Therefore, the Commission cannot constitutionally petition the courts directly for enforcement of its subpoena, but must request authorization from either the Department of Justice or some other representative of the Executive Branch.

The court rejected this argument and held that the congressional grant of investigatory power to the SEC and the concomitant power to request enforcement of its subpoenas were well within the scope of the proper delegation of constitutional authority. Indeed, investing this authority with the SEC, Congress had determined that the power to seek judicial enforcement of its orders was crucial to the effective administration of the agency’s responsibilities.

In *SEC v. Bilzerian*,^{ccxxii} Bilzerian argued that an SEC civil action that sought to enjoin violations of the federal securities laws and disgorgement of assets subsequent to an investigation was an unconstitutional delegation of executive power. The Court found that the separation of powers was not violated by executive delegation of enforcement power to the SEC, because the President retains sufficient control over the agency, and Congress “has no power or control over the enforcement activities of the SEC.” The court also noted that the President retains the power to remove a commissioner for inefficiency, neglect of duty, or malfeasance in

office, and therefore had sufficient control over the SEC to ensure that the securities laws were “faithfully executed” in accordance with Article 2, § 3 of the U.S. Constitution.

Similarly, in *SEC v. Davis*,^{ccxxiii} a defendant moved to dismiss a complaint for lack of subject matter jurisdiction alleging that the civil enforcement authority of the SEC constituted an unconstitutional delegation of executive authority because the Commission is not required to obtain approval of some official or agency within the Executive Branch prior to bringing a civil injunctive enforcement action.

The court held that the SEC’s exercise of civil enforcement responsibility did not constitute an unconstitutional delegation of authority, because Congress did not retain legislative control over the enforcement activities of the SEC, nor did it retain the power to appoint or remove commissioners.^{ccxxiv}

XXXVI. Freedom of Information Act

Documents turned over to the Commission are presumed to be subject to disclosure under the Freedom of Information Act (“FOIA”) unless a narrow range of exemptions are claimed by the Commission.^{ccxxv} Indeed, under the FOIA, the government has the burden of justifying the records’ nondisclosure.^{ccxxvi} How, then, can a corporation protect itself from unwarranted disclosure by the Commission of records produced during an SEC investigation?

The only current available means of protecting documents submitted to the staff is found in the Commission’s rules. Under 17 C.F.R. § 200.83 (1991), the Commission has provided a procedure for persons submitting information to it to request confidential treatment for that information. Pursuant to that procedure, a party submitting documents to the Commission must first segregate documents for which confidential treatment is requested from

documents for which it is not requested. Second, the documents for which confidential treatment is requested must be appropriately marked as confidential. Finally, the documents must be accompanied by a written request for confidential treatment.

The rules provide that when marking the documents, the person submitting the records must affix a prominent stamp, typed legend, or other suitable form of notice on each page stating “Confidential Treatment Requested by [name].” If that is impractical, a cover sheet prominently marked “Confidential Treatment Requested by [name]” should be fastened to each group of records submitted for which confidential treatment is requested. Each document so marked must be stamped with a separate identifying number.

Documents thus marked should then be submitted to the Commission with a written request for confidential treatment. In addition, a copy of the request should be sent to the Freedom of Information Act Officer, Securities and Exchange Commission, Washington, D.C. 20549. The written request must be identified on the envelope and on the top of the first page by the legend “FOIA Confidential Treatment Requested.” Finally, the written request must contain the name, address, and telephone number of the requester.

The rules recognize the impracticality of submitting a written request for confidential treatment when documents are submitted to the Commission during the course of testimony. In that case, the person submitting the materials must inform the Commission’s staff receiving the documents of his intent to request confidential treatment, and then submit a written confidentiality request within 30 days.

The Commission will not determine the validity of the request for confidential treatment at the time it first receives the documents. That determination will be made at the time

a FOIA request is received. Upon receipt of a request, the Commission will then determine whether one of the nine statutory exemptions to the FOIA apply.

Of these nine exemptions, the one that will most frequently apply is exemption seven, which allows the Commission to withhold records if production could reasonably be expected to interfere with enforcement activities.^{ccxxvii} Once the Commission's inquiry is concluded, and it has no further law enforcement interest in the documents, however, exemption seven is rendered inapplicable since the release of the documents no longer will interfere with law enforcement proceedings.^{ccxxviii}

It is at this time—the conclusion of the investigation—that the risk of disclosure is greatest. At that stage, the Commission's task is done and it has little interest, if any, in claiming a FOIA exemption that may embroil it in litigation. Indeed, in *Chrysler Corp. v. Brown*,^{ccxxix} the Supreme Court held that the existence of an exemption does not impose an affirmative obligation on an administrative agency to claim the exemption. While the FOIA exemptions set the limits for mandatory agency disclosure, they do not foreclose disclosure. The Commission's natural tendency will be to turn over the records of the corporation without a second thought as to their sensitivity or confidentiality.

However, if the corporation has followed the procedures outlined above for claiming confidential treatment for its documents, it will be notified by the Commission's Freedom of Information Act officer that a FOIA request has been received and it will be asked to substantiate its request for confidential treatment within ten days. If the party who submitted the corporation's documents has not requested confidential treatment, the Commission will presume that the submitter has waived any interest in asserting an exemption from disclosure under the

FOIA.^{ccxxx} Consequently, it is imperative that a confidentiality request accompany any documents submitted to the Commission. Even if the corporate requester does not believe the need for confidentiality can be substantiated, the existence of the request will at least cause the Commission to alert the submitter if a FOIA disclosure inquiry occurs.

When submitting a statement of substantiation for confidential treatment, the person seeking to maintain confidentiality must identify the specific exemptive provisions of the FOIA or the specific statutory or regulatory provisions that apply.^{ccxxx} Any applicable prior determination by the Commission, other federal agencies, or the courts concerning confidential treatment of the information also should be cited.^{ccxxxii} Moreover, the statement should include the measures taken to protect the confidentiality of the documents and describe the adverse effect of disclosure on the corporation's competitive position.^{ccxxxiii} The ease or difficulty of a competitor's obtaining or compiling the information should also be disclosed.^{ccxxxiv} Additionally, the person seeking to substantiate a claim of confidentiality must state whether the documents were voluntarily submitted to the Commission and discuss whether disclosure would tend to impede the availability of similar information to the Commission.^{ccxxxv}

Obviously, any statement substantiating the confidentiality request will require a detailed analysis of the documentation and materials for which confidentiality is sought. Since this analysis itself may be disclosed, the person submitting the statement of substantiation for confidentiality should include a statement as to the portion or portions of the substantiation which should be afforded confidential treatment.^{ccxxxvi}

After following this laborious procedure, the Commission's Freedom of Information Act officer may still determine that confidential treatment is not warranted. In which case, the

party seeking confidentiality may appeal to the Commission’s General Counsel within ten days of the date of notice of an adverse determination.^{ccxxxvii}

The appeal must be in writing and contain the same type of information originally submitted. If an adverse determination is made by the General Counsel, the party seeking information may within ten days commence an action in federal court concerning the determination to make the information or documents available.^{ccxxxviii}

If the party seeking to maintain confidentiality fails to appeal within ten days after an adverse determination at any stage, the documents will be released. An extension of the ten-day limit may be granted at the discretion of the Commission, its General Counsel, or the FOIA officer.^{ccxxxix}

As we have seen, when substantiating a request for confidentiality, it is necessary to point out the particular FOIA exemption that applies. After a Commission investigation has been concluded, there remains only one exemption that will provide any basis for barring disclosure—exemption four. That exemption provides that the FOIA does not apply to “trade secrets and commercial or financial information obtained from a person and privileged or confidential” information.^{ccxli} While this exemption may at first blush appear to provide the necessary protection for corporate records, the narrow construction placed on FOIA exemptions^{ccxli} has transformed it into a false hope.

First, before the exemption can be invoked, the document in question must contain a trade secret or confidential commercial or financial information or be privileged. This will eliminate the vast bulk of the documents that were produced during the investigation, such as letters, transmittal memoranda, and personal notes. Second, very few documents will qualify for

trade secret status, which has been defined as an “unpatented, secret, commercially valuable plan, appliance, formula or process, which is used for making, preparing, compounding, treating or processing of articles or materials which are trade commodities.”^{ccxlii} Third, the term “privilege” is generally construed to be related to common law privilege.^{ccxliii}

Thus, the only viable means of protecting documents under exemption four is to claim that the documents contain confidential commercial or financial information. However, the courts have defined this term so narrowly as to render it meaningless. In *National Parks & Conservation Ass’n v. Morton*,^{ccxliv} the District of Columbia Circuit held that before documents may be considered confidential, commercial, or financial information, a two-prong test must be met. Disclosure of information must be shown to have either of the following likely effects: (1) to impair the government’s ability to obtain necessary information in the future; or (2) to cause substantial economic harm to the competitive position of the person from whom the information was obtained.

Since the Commission can subpoena records, the first prong of the test will almost never be met. With respect to the second prong of the test, it is often difficult to prove that disclosure will cause substantial economic harm to a competitive position. Consequently, the Commission’s elaborate procedures for requesting confidential treatment provide illusory rather than real protection for documents. Thus, the passage of the FOIA, notwithstanding the Commission’s confidentiality rules, has left businesses that submit information to the Commission pursuant to an investigation with few, if any, effective avenues of legal recourse to prevent disclosure.

However, at least one vehicle exists that may lead to some, albeit minimal, shelter. A company complying with an SEC investigation should ask for the prompt return of its documents immediately following the conclusion of the investigation. The FOIA does not obligate agencies to retain documents; it only obligates them to provide access to those that it has, in fact, created and retained.^{ccxlv} The FOIA requires the Commission to disclose only those “agency records” over which it retains custody and control.^{ccxlv} Where the Commission no longer retains custody and control of business documents at the time of a FOIA request, it has no obligation to recover or produce those documents.^{ccxlvii}

As an informal matter of practice, before returning any documents, the Commission’s Division of Enforcement will first check with the Commission FOIA officer to determine if any FOIA requests have been made for the documents within the preceding six months. If there is a pending request, then the Commission is obligated to determine whether the documents must be disclosed. If, on the other hand, no request has been made nor renewed within the preceding six months, the documents may be returned.^{ccxlviii}

XXXVII. Right to Financial Privacy

Under the Right to Financial Privacy Act (RFPA or Act),^{ccxlix} the SEC may obtain “financial records” of a customer of a bank or a financial institution only under certain specified conditions: customer authorization, customer notice, or *ex parte* application to a U.S. district court.

In the absence of customer authorization,^{ccli} the Commission may issue an administrative subpoena to the bank or financial institution if there is reason to believe the records sought are relevant to a legitimate law enforcement inquiry.^{ccli} In that case, the Commission must serve

or mail a copy of the subpoena sent to the bank or financial institution to the customer, together with a notice stating with reasonable particularity the nature of the law enforcement inquiry. Within ten days of service or 14 days of mailing the notice, the customer may move to quash the subpoena in a U.S. district court with a supporting affidavit stating that “the applicant is a customer of the financial institution from which financial records pertaining to him have been sought; and stating the reasons for believing the financial records sought are not relevant to the legitimate law enforcement inquiry stated by the government authority in the notice or that there has not been substantial compliance” with the Act.^{cclii}

Once the customer has made this showing, the court “shall order the [SEC] to file a sworn response.”^{ccliii} If the court is unable to determine the motion or application on the basis of the parties’ initial allegations and responses, the court may conduct such additional proceedings as it deems appropriate.^{ccliv} “If the court finds that there is a demonstrable reason to believe that the law enforcement inquiry is legitimate and a reasonable belief that the records sought are relevant to the inquiry, it shall deny the motion If the court finds that there is no demonstrable reason to believe that the lawful enforcement inquiry is legitimate and a reasonable belief that the records sought are relevant to that inquiry . . . it shall order the process quashed.”^{cclv}

Customer authorization or the above procedure are the only means by which the Commission can gain access to financial records with one narrow exception. The SEC can obtain records without prior authorization or notice to the customer upon *ex parte* showing to an appropriate U.S. district court, if it meets the circumstances specified in § 21 of the Securities and Exchange Act.^{cclvi} A failure by the Commission to comply with the Act’s procedures has resulted in its being enjoined.^{cclvii}

In order for the customer to prevail and quash a subpoena for financial records, the customer must show a factual basis for his conclusion that the records are irrelevant. In its response, the SEC need not show there is probable cause to believe a violation has occurred but a good reason to investigate, *i.e.*, a reasonable belief that the records are relevant to the inquiry. If the Commission can show that the customer is connected to an activity that it is charged with investigating, it will have discharged its obligation under the RFPA.^{cclviii}

XXXVIII. Conclusion

The current state of the law with respect to SEC investigations generally is favorable to the Commission's ability to gather evidence efficiently and with the speed necessary to protect the public. However, the Task Force's recommendations comprise a legitimate attempt to improve the balance between the Commission's needs and the rights of witnesses and targets of investigation.

ⁱ 42 Bus. Law. 789 (May 1987).

ⁱⁱ Section 20(a) of the Securities Act of 1933 (Securities Act) (15 U.S.C. § 77t); § 21(a) of the Securities Exchange Act of 1934 (Exchange Act) (15 U.S.C. § 78u(a)); § 18(a) of the Public Utility Holding Company Act of 1935 (15 U.S.C. § 79r(a)); § 321(a) of the Trust Indenture Act of 1939 (15 U.S.C. § 77u(a)); § 42(a) of the Investment Companies Act of 1940 (15 U.S.C. § 80a-41(a)); § 209(a) of the Investment Advisers Act of 1940 (15 U.S.C. § 80b-9(a)).

Under § 8(e) of the Securities Act (15 U.S.C. § 77h(e)), the Commission is empowered to conduct an examination to determine whether a stop order should issue. The statute provides that failure to cooperate with the examination is grounds for the issuance of a stop order. Under Rule 14a-6(e) (17 C.F.R. § 240.14a-6(e)), the Commission may make such inquiries or investigations in regard to preliminary proxy material as it deems necessary for adequate review.

ⁱⁱⁱ 17 C.F.R. § 202.5(a); "Even if one were to regard [a] request for information -- as caused by official curiosity, nevertheless law-enforcing agencies have a legitimate right to satisfy themselves that corporate behavior is consistent with the law and the public interest." *United States v. Morton Salt Co.*, 338 U.S. 632, 652 (1950).

^{iv} "Blue sheets" were requests forwarded to a broker-dealer asking it to identify the purchasers and sellers of an identified security. The name "blue sheet" derives from the color of the paper the questionnaire was printed on. In the age of computers, the staff no longer makes its requests by paper. The requests are now electronically submitted and the responses are computer-generated print-outs. But, the name "blue sheets" has survived.

^v 17 C.F.R. § 202.5(a).

^{vi} 17 C.F.R. § 203 *et seq.*

^{vii} *Id.*

^{viii} *United States v. Powell*, 379 U.S. 48 (1964). *Powell* involved the enforcement of an IRS summons. However, in *SEC v. ESM Government Securities, Inc.*, 645 F.2d 310, 313-14 (5th Cir. 1981), the Fifth Circuit assumed the standards applicable to IRS summons were also applicable to SEC subpoenas. And, in *EEOC v. K-Mart Corp.*, 694 F.2d 1055, 1066 (6th Cir. 1982), the court without citation stated that *Powell* had been applied in subpoena enforcement actions brought by the EEOC, the IRS, and the SEC. See also *SEC v. Howatt*, 525 F.2d 226, 229 (1st Cir. 1975); *SEC v. Blackfoot Bituminous, Inc.*, 622 F.2d 512, 514-15 (10th Cir. 1980); *SEC v. Orton*, 100 F.3d 968 (10th Cir. 1996), *cert. denied*, 117 S. Ct. 2435 (1997); *United States v. Sturm, Ruger & Co.*, 84 F.3d 1, 5 (1st Cir. 1996)(where the court held that "[a]s long as the agency's assertion of authority is not obviously apocryphal, a procedurally sound subpoena must be enforced.").

In *Howatt*, 525 F.2d at 226, the court, citing *Powell*, held that the Commission must show that the inquiry is for a proper purpose, the information sought is relevant, and the statutory procedures observed. It did not mention or discuss *Powell's* fourth element -- that the information is not already possessed by the government. In *SEC v. Wheeling-Pittsburgh Steel Corp.*, 648 F.2d 118, 128 (3d Cir. 1981), the majority stated that *Powell's* four-part showing is applicable to all agency enforcement proceedings. At the same time, the court suggested that a subpoena may be challenged on any appropriate ground and that district courts may deny enforcement under their equitable powers. *Id.* at 125, 128.

It should be noted that cases relating to IRS subpoenas may not apply to every aspect of the law regarding Commission subpoenas. See generally *SEC v. ESM Gov. Sec. Inc.*, 645 F.2d at 313; *SEC v. Dresser Indus., Inc.*, 628 F.2d 1368 (D.C. Cir. 1980).

^{ix} Section 19(b) of the Securities Act (15 U.S.C. § 77s(b)); § 21(b) of the Exchange Act (15 U.S.C. § 78u(b)); § 18(c) of the Public Utility Holding Company Act of 1935 (15 U.S.C. § 79r(c)); § 321(a) of the Trust Indenture Act of 1939 (15 U.S.C. § 77(a)); § 42(b) of the Investment Companies Act of 1940 (15 U.S.C. § 80-41(b)); § 209(b) of the Investment Advisers Act of 1940 (15 U.S.C. § 80b-9(b)).

^x *Gordon v. SEC*, [1980 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 97,628 (N.D. Ga. 1980); see also *Kixmiller v. SEC*, 492 F.2d 641 (D.C. Cir. 1974); *Dyer v. SEC*, 291 F.2d 774 (8th Cir. 1961).

^{xi} However, there is no statutory restriction on the Commission's power to subpoena third parties not named in the formal order who may have materials relevant to the inquiry. *SEC v. Horowitz & Ullman P.C.*, [1981-1982 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 98,488 at 92,861 (N.D. Ga. 1982).

^{xii} The Commission, however, is not bound by the areas mentioned in its formal order and the staff is free to inquire into whatever areas the investigation leads. *SEC v. ESM Gov. Sec., Inc.*, [1979 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 96,850 at 4 (S.D. Fla. 1979).

^{xiii} See *supra* note 3 and accompanying text.

^{xiv} *SEC v. Arthur Young & Co.*, 584 F.2d 1018, 1026-27 (D.C. Cir. 1978); 15 U.S.C. § 78d-l(a).

^{xv} *International Waste Controls, Inc. v. SEC*, 362 F. Supp. 117, 119 (S.D.N.Y. 1973), *aff'd*, 485 F.2d 1238 (2d Cir. 1973) (*per curiam*); *Stardust, Inc. v. SEC*, 225 F.2d 255 (9th Cir. 1955); see also *State, Dept. of Commerce & Ins. v. First Trust Money Servs., Inc.*, 931 S.W.2d 226, 228 (Tenn. Ct. App. 1996).

^{xvi} *International Waste Controls*, 362 F. Supp. at 120; *M.G. Davis & Co. v. Cohen*, 369 F.2d 360, 362-63 (2d Cir. 1966); *Gellis v. Casey*, 338 F. Supp. 651, 652-53 (S.D.N.Y. 1972); see also *State, Dept. of Commerce &*

Ins., 931 S.W.2d at 228; *SEC v. Sayegh*, [1996-1997 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 99,068 (S.D.N.Y. 1996).

^{xvii} See *Hannah v. Larche*, 363 U.S. 420 (1960); *Gold v. SEC*, 48 F.3d 987, 992 (7th Cir. 1995); *RNR Enters., Inc. v. SEC*, 122 F.3d 93, 98 (2d Cir. 1997); *Wells v. SEC*, 113 F.3d 1230 (2d Cir.), *cert. denied*, 118 S. Ct. 386 (1997); *Popovic v. United States*, 997 F. Supp. 672, 678 (D. Md. 1998).

^{xviii} *Id.* at 446.

^{xix} *United States v. Morton Salt Co.*, 338 U.S. at 642.

^{xx} *SEC v. Meek*, [1979-1980 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 97,105 (W.D. Okla. 1979), *aff'd*, [1979-1980 Transfer Binder] Fed. Sec. L. Rep. (CCH) 97,323 (10th Cir. 1980) (*per curiam*).

^{xxi} *SEC v. Jerry T. O'Brien, Inc.*, 467 U.S. 735 (1984); see also *RNR Enters., Inc. v. SEC*, 122 F.3d at 98; *Wells*, 1997 WL 274270, at *2.

^{xxii} *SEC v. Isbrandtsen*, 245 F. Supp. 518, 521 (S.D.N.Y. 1965).

^{xxiii} 17 C.F.R. § 203 *et seq.*

^{xxiv} 17 C.F.R. § 203.7(a).

^{xxv} 17 C.F.R. § 203.7(b).

^{xxvi} *SEC v. Csapo*, 533 F.2d 7 (D.C. Cir. 1976); *SEC v. Higashi*, 359 F.2d 550 (9th Cir. 1966).

^{xxvii} *SEC v. Whitman*, 613 F. Supp. 48 (D.D.C. 1985).

^{xxviii} 17 C.F.R. § 203.6; *Commercial Capital Corp. v. SEC*, 360 F.2d 856 (7th Cir. 1966); see also *Greer v. New Jersey Bureau of Sec.*, 677 A.2d 763, 765 (N.J. Super. Ct. App. Div. 1994).

^{xxix} 17 C.F.R. § 203.6; *SEC v. Sprecher*, 594 F.2d 317, 319 (2d Cir. 1979).

^{xxx} *Id.*; *Cf. Thomas v. Shultz*, 107 F.R.D. 624 (D.D.C. 1985).

^{xxxi} 18 U.S.C. § 3500 requires that, in a criminal case, the government must turn over a witness's statement when that witness has testified on direct examination for the government.

^{xxxii} *United States v. Lieberman*, 608 F.2d 889 (1st Cir. 1979); see also *United States v. Houlihan*, 92 F.3d 1271, 1288 (1st Cir. 1996) *petition for cert. filed* (U.S. Jan. 18, 2000) (No. 99-10205) (the Jenks Act does not impose an obligation on government agents to record witness interviews or to take notes during such interviews), *cert. denied*, 117 S. Ct. 963 (1997); *United States v. Brimage*, 115 F.3d 73, 76 (1st Cir.) (the government is not required to record all aspects of interviews with witnesses), *cert. denied*, 118 S. Ct. 321 (1997).

^{xxxiii} Section 19(b) of the Securities Act (15 U.S.C. § 77s(b)); § 21(b) of the Exchange Act (15 U.S.C. § 78u(b)); § 42(b) of the Investment Exchange Act (15 U.S.C. § 80a-41(b)); § 209(b) of the Investment Advisers Act, 15 U.S.C. § 80b-9(b).

^{xxxiv} 17 C.F.R. §§ 203.8, 201.14(b)(3). When the subpoena is served by registered or certified mail, service is valid where the witness receives notice, even if the return receipt is not signed by him. *NLRB v. Strickland*, 220 F. Supp. 661 (W.D. Tenn. 1962), *aff'd*, 321 F.2d 811 (6th Cir. 1963).

^{xxxv} 17 C.F.R. § 201.14(b)(3)(ii).

^{xxxvi} 28 U.S.C. § 1783(b).

^{xxxvii} *Commodity Futures Trading Comm'n v. Nahas*, 738 F.2d 487 (D.C. Cir. 1984); *SEC v. Zanganeh*, 470 F. Supp. 1307 (D.D.C. 1978).

^{xxxviii} *Societe Nationale Industrielle Aerospatiale v. United States Dist. Court for S. Dist. of Iowa*, 482 U.S. 522 (1987); *Societe Internationale Pour Participations Industrielles et Commerciales, S.A. v. Rogers*, 357 U.S. 197, 204-06 (1958); *In Re Uranium Antitrust Litigation*, 480 F. Supp. 1138, 1144-45 (N.D. Ill. 1979).

In *Societe Nationale Industrielle Aerospatiale*, the Supreme Court considered how a district court should resolve conflicts between the application of the Federal Rules of Civil Procedure and the Hague Convention on the Taking of Evidence Abroad in Civil or Commercial Matters. While acknowledging the power of the court to order a foreign national party before it to produce evidence physically located abroad, the Court directed district courts to determine whether the Hague Convention's procedure should be utilized in lieu of discovery under the Federal Rules after "scrutiny in each case of the particular facts, sovereign interests, and likelihood that resort to these procedures would prove effective." 482 U.S. at 544. The Court acknowledged that the Hague Convention is "intended as a permissive supplement, not a preemptive replacement, for other means of obtaining evidence located abroad." *Id.* at 536.

^{xxxix} *SEC v. Banca Della Svizzera Italiana*, 92 F.R.D. 111 (S.D.N.Y. 1981).

^{xl} There is a distinction in the standard the court must apply in deciding whether to require production and the standard it applies in determining whether to impose sanctions for noncompliance once production has been ordered." *Societe Internationale Pour Participations*, 357 U.S. 197 (1958); *Ohio v. Arthur Andersen & Co.*, 570 F.2d 1370, 1372 (10th Cir. 1978); *Arthur Andersen & Co. v. Finesilver*, 546 F.2d 338, 341 (10th Cir. 1976); *Soletanche & Rodio, Inc. v. Brown & Lambrecht Earth Movers, Inc.*, 99 F.R.D. 269 (N.D. Ill. 1983); *In re Uranium Antitrust Litigation*, 480 F. Supp. at 1147-48; *see also Bank of New York v. Meridien BIAO Bank Tanzania Ltd.*, 171 F.R.D. 135, 153 (S.D.N.Y. 1997). At the first stage, the court must balance the various competing interests in determining whether to order productions. In *United States v. Vetco Inc.*, 691 F.2d 1281 (9th Cir. 1981), the court balanced the factors set forth in § 40 of the RESTATEMENT (SECOND) OF THE FOREIGN RELATIONS LAW OF THE UNITED STATES (1965), and concluded that the possibility of criminal liability in Switzerland did not preclude enforcement and sanctions; *Cf. Cochran Consulting, Inc. v. Uwatec USA, Inc.*, 102 F.3d 1224 (Fed. Cir. 1996). In *Garpeg Ltd. v. United States*, 583 F. Supp. 789 (S.D.N.Y. 1984), the court also adopted the balancing approach of § 40, holding that an IRS summons should be enforced despite possible complications with Hong Kong's secrecy laws. *See also Minpeco, S.A. v. Conticommodity Servs., Inc.*, 653 F. Supp. 957 (S.D.N.Y.), *aff'd*, 832 F.2d 739 (2d Cir. 1987), in which the court held that the balancing of the relevant factors did not compel disclosure of information protected by Swiss bank secrecy laws. In *In re Uranium Antitrust Litigation*, 480 F. Supp. at 1148, the court found the balancing test of § 40 unworkable and looked at these factors in striking its balance: (1) the importance of the policy underlying the statute forming the basis of the plaintiff's claim; (2) the importance of the requested documents; and (3) the foreign nation's flexibility in applying its nondisclosure law. In balancing the competing interests of the United States and the foreign state, the court will also consider whether a governmental agency, rather than a private party, has requested the information. *United States v. Davis*, 767 F.2d 1025 (2d Cir. 1985); *see also Machado & Co. v. Cafe de Chiapas, S.A. de C.V.*, No. 94 CIV. 3935 (JFK), 1994 WL 406164 (S.D.N.Y. Aug. 01, 1994).

At the second stage, the court must examine the party's good faith efforts to comply before imposing sanctions. *Societe Internationale Pour Participations*, 357 U.S. at 204-06. In *United States v. Hayes*, 722 F.2d 723 (11th Cir. 1984), the court held that a party seeking to avoid a contempt order on the ground that the subpoenaed records were located in Switzerland had not shown that he had in good faith made "all reasonable efforts to comply." *See also In re Grand Jury Proceedings*, 691 F.2d 1384 (11th Cir. 1982). On the other hand, the court in *In re Westinghouse Elec. Corp. Uranium Contracts Litigation*, 563 F.2d 992 (10th Cir. 1977), relieved a party from a contempt order where it was shown that a good faith effort at compliance had been made. *See also Richmark Corp. v. Timber Falling Consultants*, 959 F.2d 1468, 1475 (9th Cir. 1992); *RNW Assocs., Inc. v. Corporate Underwriters, Ltd.*, 45 F.3d 440 (10th Cir. 1994). In *In re Sealed Case*, 825

F.2d 494 (D.C. Cir. 1987), after examining the dilemma in which a non-target bank found itself, the court refused to enter a civil contempt order which would compel the bank to violate the laws of a foreign country. The court felt it unfair to subject the bank to criminal liability when it could not control the situation. On the other hand, it ordered the bank manager, who could avoid foreign prosecution by remaining in the United States, to testify. *See also SEC v. Bankers Alliance Corp.*, 881 F. Supp. 673 (D.D.C. 1995), *reconsidered in* No. C.A. 95-0428 (PLF), 1995 WL 590665 (D.D.C. 1995).

The distinction between these standards has often been blurred. Thus, the courts have discussed the balancing factors of § 40 together with the good faith standard at either or both stages. At least one court has suggested that the distinction has little practical effect. *SEC v. Banca Della Svizzera Italiana*, 92 F.R.D. at n.32. While the court is undoubtedly correct about the distinction's practical effect, it is a useful analytical tool.

^{xli} *SEC v. Isbrandtsen*, 245 F. Supp. 518, 520 (S.D.N.Y. 1965), *see supra* note 22; *see also People's Bank v. Williams*, 449 F. Supp. 254, 260-61 (W.D. Va. 1978); *Reisman v. Caplin*, 375 U.S. 440 (1964); *Couch v. United States*, 409 U.S. 322 (1973).

^{xlii} *Bird v. SEC*, [1980 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 97,506 (C.P.R. 1980). There are no administrative procedures for moving to quash an SEC subpoena internally. *Panaro v. SEC*, [1987 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 93,368 (E.D.N.Y. 1987). In *Fleet/Norstar Financial Group, Inc. v. SEC*, 769 F. Supp. 19 (D. Me. 1991), the court reiterated the long-standing rule that SEC subpoenas, which are not self-executing and contain no sanction for failure to comply, may not be challenged in a federal court by way of a motion to quash. Congress has provided the exclusive form in which the plaintiff may secure full adjudication of its objection to the subpoena, *i.e.*, an enforcement action brought in the U.S. District Court by the SEC for failure to comply. In *Garvin v. SEC*, [1993-1994 Transfer Binder] Fed. Sec. L. Rep. ¶ 98,126, the court held that an individual could not rely on the Right to Financial Privacy Act of 1978 to quash a subpoena served by the SEC for certain personal bank records. Absent a claim that subpoenaed documents were irrelevant to the investigation or that the government failed to comply with the Act, the subpoena will be upheld. *See Reisman*, 375 U.S. at 445-46; *see also Atlantic Richfield Co. v. FTC*, 546 F.2d 646, 648-50 (5th Cir. 1977); *Lopes v. Resolution Trust Corp.*, 155 F.R.D. 14 (D.R.I. 1994); *Mackey v. SEC*, No. 3:96MC407, 1997 WL 114801 (D. Conn. Feb. 21, 1997).

^{xliii} 133 F.R.D. 115 (N.D. Ill. 1990); *see also SEC v. Softpoint, Inc.*, 958 F. Supp. 846, 857 (S.D.N.Y. 1997), *aff'd*, 159 F.3d 1348 (2d Cir. 1998).

^{xliv} *See Reisman*, 375 U.S. at 440; *SEC v. Andrews*, 88 F.2d 441 (2d Cir. 1937); *First Jersey Sec., Inc. v. SEC*, 553 F. Supp. 205 (D.N.J. 1982); *People's Bank*, 449 F. Supp. at 254; *Maschler v. National Ass'n of Sec. Dealers, Inc.*, 827 F. Supp. 131, 132 (E.D.N.Y. 1993); *Hunter v. SEC*, 879 F. Supp. 494, 500-02 (E.D. Pa. 1995).

^{xlv} *See United States v. Morton Salt Co.*, 338 U.S. at 652; *SEC v. Arthur Young & Co.*, 584 F.2d at 1018. In *Blinder, Robinson & Co. v. SEC*, 692 F.2d 102 (10th Cir. 1982), *aff'd*, 748 F.2d 1415 (1984), a broker-dealer sought to enjoin a Commission investigation that, it contended, had been conducted with unlimited power and for an unlimited time. The district court held that the action was rendered moot by virtue of the Commission filing an enforcement proceeding against the broker. The circuit court reversed and remanded on the ground that the formal order of investigation was still outstanding and the Commission could thus resume its investigation. Although the court conceded that an order initiating an investigation is interlocutory and not reviewable until a final order is entered as a result of the investigation, a judicial challenge to the statutory power of the Commission to investigate could be made.

^{xlvi} *SEC v. F.N. Wolf & Co.*, [1993-1994 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 98, 015. In *Hunter v. SEC*, [1994-1995 Transfer Binder] Fed. Sec. L. Rep. ¶ 98, 402, an individual could not obtain a temporary restraining order based on a claim that he was investigated for improper reasons when one of the investigators was romantically involved with the individual's former girlfriend and was uncovering information that would benefit the former girlfriend and the investigator.

^{xlvii} *First Jersey Sec., Inc. v. SEC*, 476 A.2d 861 (N.J. Super. Ct. App. Div. 1984). Federal district courts have exclusive jurisdiction, and state courts lack jurisdiction to enjoin compliance with a Commission subpoena. *Boyce Box v. Amarillo Nat'l Bank*, [1979 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 96,905 (N.D. Tex. 1979). In addition, state law may not interfere with the enforcement of a Commission subpoena. *SEC v. First Tenn. Bank N.A. Memphis*, 445 F. Supp. 1341 (W.D. Tenn. 1978). In *SEC v. Pacific Bell*, 704 F. Supp. 11 (D.D.C. 1989), the staff subpoenaed telephone toll records from Pacific Bell which refused to produce them on the grounds that the SEC had not obtained consent to the release of the requested record as required by the California Customer Right of Privacy Act. Cal Pub. Util. Code § 2891(a) (West 1992). The court held that to the extent California law conflicted with the federal securities laws and regulations, under the supremacy clause of the U.S. Constitution, the California law is preempted by federal law.

^{xlviii} *Treats Int'l Enters. Inc. v. SEC*, 828 F. Supp. 16 (S.D.N.Y. 1993) (the court denied a preliminary injunction because enjoinderment was beyond the scope of review for abuse of agency discretion and the SEC made at least a minimal showing of good faith); see also *AVCO Fin. Corp. v. CFTC*, 929 F. Supp. 714, 723 (S.D.N.Y. 1996).

^{xlix} *SEC v. Sprecher*, 594 F.2d 317 (2d Cir. 1979).

¹ *Donaldson v. United States*, 400 U.S. 517(1971); see also *EEOC v. St. Regis Paper Co.-- Kraft Div.*, 717 F.2d 1302 (9th Cir. 1983); *United States v. Thriftyman, Inc.*, 704 F.2d 1240 (Emer. App. 1983).

ⁱⁱ *United States v. Powell*, 379 U.S. 48, 48 (1964); *SEC v. Blackfoot Bituminous, Inc.*, 622 F.2d 512, 515 (10th Cir. 1980); *SEC v. Howatt*, 525 F.2d 226, 229 (1st Cir. 1975); see *supra* note 8 and accompanying text.

ⁱⁱⁱ See *supra* note 8 and accompanying text.

ⁱⁱⁱⁱ *United States v. Morton Salt Co.*, 338 U.S. at 652; see *SEC v. Blinder, Robinson & Co.*, 681 F. Supp. 1 (D.D.C. 1987).

^{lv} *SEC v. Horowitz & Ullman, P.C.*, [1981-1982 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 98,488, ¶ 98,488 (N.D. Ga. 1982); see also *supra* note 11.

^{lv} *SEC v. Jerry T. O'Brien*, 467 U.S. 735, 747 & n.18 (1984); see *supra* note 21.

^{lvi} In *SEC v. Blackfoot Bituminous, Inc.*, 622 F.2d at 515, the court addressed but refused to decide whether this requirement of *Powell* applied because the Commission made a "facially" valid showing that it did not have the information requested. In *SEC v. Horowitz & Ullman, P.C.*, Fed. Sec. L. Rep. (CCH) at ¶ 98,488, the court suggested that this requirement of *Powell* may not apply to Commission investigations. It then went on to say that if this requirement is applicable, it is not absolute and the court must weigh the interests of the Commission and the party subpoenaed.

The Commission will rarely subpoena documents already in its possession. It may and does subpoena the same documents from different parties in order to ascertain if there are different versions or marginal notations. It is unlikely that a court would hold that the Commission is already in possession of the document under such circumstances and deny enforcement under *Powell*. Indeed, it has been held that the fact that the Commission can obtain the information from another source does not prevent it from issuing and enforcing a subpoena. *SEC v. Murray Dir. Affiliates, Inc.*, 426 F. Supp. 684 (S.D.N.Y. 1976).

^{lvii} See *In re EEOC*, 709 F.2d 392, 400 (5th Cir. 1983); *SEC v. Wheeling-Pittsburgh Steel Corp.*, 648 F.2d at 128; see also *supra* note 8.

^{lviii} *Oklahoma Press Publ'g Co. v. Walling*, 327 U.S. 186 (1946); *United States v. Morton Salt Co.*, 338 U.S. at 632; *SEC v. Brigadoon Scotch Distrib. Co.*, 480 F.2d 1047 (2d Cir. 1973); *SEC v. Wall Street Transcript Corp.*, 422 F.2d 1371, 1375 (2d Cir. 1970) ("[I]t has long been established that the question of the inclusion of a particular person or entity within the coverage of a regulatory scheme is generally for initial determination by

an agency, subject to review on direct appeal, rather than for a district court whose jurisdiction is invoked to enforce an administrative subpoena.") *SEC v. Savage*, 513 F.2d 188 (7th Cir. 1975); *SEC v. Meek*, [1979-1980 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 97,105, ¶ 97,323 (W.D. Okla. 1979); see *supra* note 20 and accompanying text; see also *Gallard v. United States Gov't*, 882 F. Supp. 1440 (S.D.N.Y. 1995); *AVCO Financial Corp. v. CFTC*, 929 F. Supp. 714, 723 (S.D.N.Y. 1996).

^{lix} *SEC v. Arthur Young & Co.*, 584 F.2d 1018 (D.C. Cir. 1978); see *supra* note 14; see also *SEC v. National Bank of Commerce*, 216 F. Supp. 932 (W.D. Wash. 1963).

^{lx} See Part IX. and X. *supra*.

^{lxi} See *SEC v. Arthur Young & Co.*, 584 F.2d at 1024-1025.

^{lxii} See *supra* note 58 and accompanying text.

^{lxiii} *SEC v. Arthur Young & Co.*, 584 F.2d at 1029.

^{lxiv} *Id.*; see also *Endicott Johnson Corp. v. Perkins*, 317 U.S. 501, 509 (1943); *SEC v. National Bank of Commerce*, 216 F. Supp. at 933; *SEC v. Kaplan*, 397 F. Supp. 564, 570 (E.D.N.Y. 1975); *In re Gimbel*, 77 F.3d 593, 598 (2d Cir. 1996); *United States v. Hunton & Williams*, 952 F. Supp. 843, 854 (D.D.C. 1997); *United States M.S.P.B. v. Geller*, No. 96 C 2768, 1997 WL 158348, at *2 (N.D. Ill. Mar. 28, 1997); *United States v. Szur*, No. 97 CR. 108 (JGK), 1997 WL 153832, at *2 (S.D.N.Y. Apr. 2, 1997). In *United States M.S.P.B. v. Geller*, the court held that the fact that the information sought is redundant with that previously obtained by the agency has no impact on the enforcement proceeding. 1997 WL 158348, at *2. The court also held that the conclusive issue in an enforcement proceeding is whether the information sought is relevant to the agency's inquiry. *Id.*

^{lxv} *S.E.C. v. Arthur Young & Co.*, 584 F.2d at 1029.

^{lxvi} *Id.*

^{lxvii} See *See v. City of Seattle*, 387 U.S. 541, 544 (1967); *United States v. Morton Salt Co.*, 338 U.S. at 652; *Oklahoma Press Publ'g Co. v. Walling*, 327 U.S. 186, 208 (1946); see *supra* note 58; see also *SEC v. Arthur Young & Co.*, 584 F.2d at 1031.

^{lxviii} *SEC v. Brigadoon Scotch Distrib. Co.*, 480 F.2d at 1056; see *supra* note 58 and accompanying text; see also *SEC v. Blackfoot Bituminous, Inc.*, 622 F.2d 512, 515 (10th Cir. 1980); see *supra* note 8 and accompanying text.

^{lxix} *Bank of Am. Nat'l Trust & Sav. Ass'n v. Douglas*, 105 F.2d 100, 107 (D.C. Cir. 1939).

^{lxx} *SEC v. Arthur Young & Co.*, 584 F.2d at 1033; see also *SEC v. Blinder, Robinson & Co.*, 681 F. Supp. 1, 1 (D.D.C. 1987). The Task Force Report would require the Commission to bear the cost of reproduction above \$100 for individuals and \$500 for other entities.

^{lxxi} *SEC v. Savage*, 513 F.2d 188, 189 (7th Cir. 1975).

^{lxxii} *SEC v. Arthur Young & Co.*, 584 F.2d at 1031-1034.

^{lxxiii} See *United States v. LaSalle Nat'l Bank*, 437 U.S. 298, 316-17 (1978); *In re EEOC*, 709 F.2d 392, 392 (5th Cir. 1983); see also *EEOC v. Michael Constr. Co.*, 706 F.2d 244 (8th Cir. 1983); *United States v. Lask*, 703 F.2d 293 (8th Cir. 1983); *SEC v. Brigadoon Scotch Distrib. Co.*, 480 F.2d at 1056; *SEC v. Wheeling-Pittsburgh Steel Corp.*, 648 F.2d at 127 ("At all times, of course, the burden is on the respondent of showing an abuse of the court's process"); see *supra* note 52; see also *United States v. Jose*, 131 F.3d 1325, 1328 (9th Cir. 1997).

^{lxxiv} *SEC v. Brigadoon Scotch Distrib. Co.*, 480 F.2d at 1056.

^{lxxv} *United States v. Lask*, 703 F.2d at 297; *EEOC v. Michael Constr. Co.*, 706 F.2d at 244.

^{lxxvi} *United States v. Powell*, 379 U.S. at 58; *see supra* note 8 and accompanying text; *see also SEC v. Brigadoon Scotch Distrib. Co.*, 480 F.2d at 1056; *United States v. LaSalle Nat'l Bank*, 437 U.S. at 298 (holding that even an illegitimate secondary purpose will not preclude enforcement in light of a legitimate purpose); *see also Tiffany Fine Arts, Inc. v. United States*, 469 U.S. 310 (1985) (holding that the showing of a secondary purpose by the Internal Revenue Service in seeking the requested material does not defeat the Service's assertions).

^{lxxvii} *SEC v. Knopfler*, 658 F.2d 25, 26 (2d Cir. 1981) (*per curiam*) (staff allegedly conducted its investigation because of prejudice against orthodox Jews); *see also RNR Enter., Inc. v. SEC*, 122 F.3d 93, 97 (2d Cir. 1997); *SEC v. F.N. Wolf & Co.*, [1993-1994 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 98,015, ¶ 98,284; *see supra* note 46.

^{lxxviii} *SEC v. E.S.M. Gov't Sec., Inc.*, 645 F.2d 310, 310 (5th Cir. 1981); *see supra* note 12.

^{lxxix} *See also United States v. Deak-Perera & Co.*, 566 F. Supp. 1398 (D.D.C. 1983) (court held that if government misleads a party into granting it access to records that would be otherwise unavailable, subsequent subpoena requesting production of those records will not be enforced).

^{lxxx} *SEC v. Wheeling-Pittsburgh Steel Corp.*, 648 F.2d at 118.

^{lxxxi} *Id.* at 129.

^{lxxxii} *See United States v. Armada Petroleum Corp.*, 562 F. Supp. 43, 51 (S.D. Tex. 1982), *aff'd*, 700 F.2d 706 (Emer. Ct. App. 1983); *United States v. Phoenix Petroleum Co.*, 571 F. Supp. 16, 20 (S.D. Tex. 1982), *aff'd*, 727 F.2d 1579 (Emer. Ct. App. 1984).

^{lxxxiii} *EEOC v. K-Mart Corp.*, 694 F.2d 1055, 1067 (6th Cir. 1982).

^{lxxxiv} *See United States v. Moon*, 616 F.2d 1043, 1047 (8th Cir. 1980) (*per curiam*); *United States v. Lask*, 703 F.2d 293, 300 (8th Cir. 1983); *United States v. Harris*, 628 F.2d 875, 883 (5th Cir. 1980); *RNR Enters., Inc. v. SEC*, 122 F.3d at 98.

^{lxxxv} *United States v. Harris*, 628 F.2d at 880.

^{lxxxvi} *See United States v. OMT Supermarket, Inc.*, 995 F. Supp. 526, 530 (E.D. Pa. 1997) (Legal conclusions, whether asserted in a brief, at oral argument, or in answer or an affidavit, in opposition to the enforcement of an IRS summons are insufficient); *SEC v. Wheeling-Pittsburgh Steel Corp.*, 648 F.2d at 128 (the party challenging the subpoena bears the initial burden of convincing the court that the claimed abuse of discretion is not frivolous); *United States v. Garden State Nat'l Bank*, 607 F.2d 61, 71 (3d Cir. 1979) (conclusions in legal memorandum insufficient); *see also United States v. Balanced Fin. Management, Inc.*, 769 F.2d 1440 (10th Cir. 1985); *Springer v. IRS*, No. S97-0091 WBS GGH, 1997 WL 732526, at *4 (E.D. Cal. Sept. 12, 1997); *SEC v. Knopfler*, 658 F.2d 25, 26 (2d Cir. 1981), *see supra* note 77.

^{lxxxvii} *SEC v. Howatt*, 525 F.2d 226, 229 (1st Cir. 1975), *see supra* note 8.

^{lxxxviii} *SEC v. Wheeling-Pittsburgh Steel Corp.*, 648 F.2d at 128.

^{lxxxix} *Id.*; *United States v. Fensterwald*, 553 F.2d 231, 232-33 (D.C. Cir. 1977) (*per curiam*); *United States v. Church of Scientology*, 520 F.2d 818, 822, 824-5 (9th Cir. 1975); *United States v. Salter*, 432 F.2d 697, 700 (1st Cir. 1970); *see also Chiu v. United States*, No. CV 96-5297-WJR (RCX), 1997 WL 331792, at *5 (C.D. Cal. Mar. 18, 1997).

^{xc} *SEC v. Wheeling-Pittsburgh Steel Corp.*, 648 F.2d at 129.

^{xc}_i *S.E.C. v. Dresser Indus., Inc.*, 628 F.2d 1368, 1388 (D.C. Cir. 1980), *see supra* note 52.

^{xc}_{ii} 111 F.3d 921 (D.C. Cir. 1997).

^{xc}_{iii} *See* 111 F.3d at 926-27. The district court relied, in part, on *Dresser*, 628 F.2d at 1388, in concluding that in the context of subpoena enforcement proceedings, discovery beyond interrogatories or affidavits is inappropriate absent extraordinary circumstances. *See S.E.C. v. Lavin*, 937 F. Supp. 23, 28 (D.D.C. 1996). Specifically, the *Dresser* court determined that such circumstances exist when a party presents some evidence that the Commission issued subpoenas in bad faith. *See* 628 F.2d at 1388. However, the D.C. Circuit observed that *Dresser* was inapposite to *Lavin* because, unlike the parties in *Dresser*, "the Lavins neither suggested that the S.E.C. had acted in bad faith nor sought discovery into the agency's investigative practices." 111 F.2d at 926.

^{xc}_{iv} *SEC v. Lockheed Aircraft Corp.*, 404 F. Supp. 651 (D.D.C. 1975); *SEC v. Boeing Co.*, [1975-1976 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 95,442 (D.D.C. 1976).

^{xc}_v 17 C.F.R. § 200.83.

^{xc}_{vi} While it is clear that there is no intervention as of right in an investigation, the circuits are split as to whether a party may intervene as of right under Rule 24(a)(2) once the Commission has commenced a civil action seeking an injunction. In *SEC v. Everest Management Corp.*, 475 F.2d 1236 (2d Cir. 1972), the Second Circuit held that intervention as of right was unavailable in a Commission civil action because the intervenors were not "so situated that the disposition of the action may as a practical matter impair or impede [their] ability to protect that interest." *Id.* at 1239. At least two district courts within the Second Circuit have interpreted the case to mean that there may be no intervention as of right in Commission civil actions. *SEC v. Canadian Javelin Ltd.*, 64 F.R.D. 648 (S.D.N.Y. 1974); *SEC v. Vesco*, 58 F.R.D. 182 (S.D.N.Y. 1974); *see also SEC v. Reed*, 97 F.R.D. 746, 749 (S.D.N.Y. 1983). However, in *SEC v. Flight Transp. Corp.*, 699 F.2d 943 (8th Cir. 1983), the Eighth Circuit held that a party can intervene as of right in an SEC civil action and distinguished *Everest Management* by explaining that case merely held that intervention as of right was only appropriate in unusual circumstances. *Id.* at 950; *see also SEC v. Prudential Sec., Inc.*, 171 F.R.D. 1, 4 (D.D.C. 1997) (section 21(g) of the Securities Exchange Act of 1934 does not bar intervention at least in post-judgment proceedings), *aff'd*, 136 F.3d 153 (D.C. Cir. 1998); *SEC v. Wozniak*, Civ. No. 92 C 4691, 1993 WL 34702, at *1 (N.D. Ill. Feb. 8, 1993) (section 21(g) operates as "an impenetrable wall" to intervention by "a victim of the same major fraudulent scheme that triggered the SEC's original filing of its own Complaint for enforcement of the securities laws."); *SEC v. Qualified Pensions, Inc.*, No. CIV. A. 95-1746-LFO, 1998 WL 29496, at *2 (D.D.C. Jan. 16, 1998).

^{xc}_{vii} *Donaldson v. United States*, 400 U.S. 517 (1971); *see supra* note 50.

^{xc}_{viii} *Id.* at 530.

^{xc}_{ix} *Id.* at 531.

^c *SEC v. Dresser Indus.*, 628 F.2d 1368, 1368 (D.C. Cir. 1980).

^{ci} *Donaldson v. United States*, 400 U.S. at 530.

^{cii} Under § 21(d), 15 U.S.C. § 78u(d), the Commission may "transmit such evidence as may be available concerning" violations of the federal securities laws "to the Attorney General, who may in his discretion institute the necessary criminal proceedings."

The Commission, by rule, also has approved the practice of the Director of the Division of Enforcement granting access to materials in the Commission's files concerning nonpublic investigations. Written

request for such access may be submitted by special counsels and other similar persons appointed in Commission litigation, the Securities Investor Protection Corporation, and trustees and counsel for trustees appointed pursuant to § 5(b) of the Securities Investors Protection Act. However, in matters in which the Commission has entered a formal order of investigation, such access may be granted only with the concurrence of the General Counsel. 17 C.F.R. § 200.30-4(a)(7); 17 C.F.R. § 203.2.

Since the Commission refers matters to the Justice Department and routinely grants it access to its files, it has been argued that an unscrupulous member of the Commission's staff might issue a Commission subpoena for the sole purpose of assisting a grand jury investigation. However, that argument has little validity since grand jury subpoenas are self-executing while Commission subpoenas are not. Therefore, there would be little advantage to be derived from issuing a Commission subpoena rather than the grand jury's own process.

^{ciii} *United States v. LaSalle Nat'l Bank*, 437 U.S. 298, 298 (1978).

^{civ} *SEC v. Dresser Industries*, 628 F.2d at 1368.

^{cv} *Id.* at 1387. In *SEC v. Rubinstein*, 95 F.R.D. 529 (S.D.N.Y. 1982), the court refused to seal all discovery to prevent disclosure to the Department of Justice because the Commission had been specifically authorized by Congress to refer evidence to the Attorney General. Previously, the Second Circuit had commended the Commission on its use of that authority in *United States v. Fields*, 592 F.2d 638, 646 & n.19 (2d Cir. 1978).

^{cvi} 936 F. Supp. 952 (S.D. Fla. 1996).

^{cvi} *Id.* at 955.

^{cvi} *See id.* at 955-56 (citing *SEC v. Dresser Indus., Inc.*, 628 F.2d at 1368). The *Incendy* court also relied upon *United States v. Kordel*, 397 U.S. 1 (1970) where the Supreme Court enumerated "special circumstances" where the contemporaneous adjudication of a criminal and civil proceeding that would cause substantial and irreparable prejudice would require a district court to postpone one of the proceedings pending the resolution of the other. *See id.* at 11-13. Examples of "special circumstances" that would warrant such action include (1) if the Government brought a civil action solely to obtain evidence for its criminal prosecution; (2) if the Government failed to advise the defendant in the civil proceeding that it contemplates his criminal prosecution; (3) if the defendant is without counsel or reasonably fears prejudice from adverse pretrial publicity or other unfair injury; or (4) any other special circumstances indicating unconstitutionality or impropriety. *Id.* at 11. The *Incendy* court hedged its reasoning, in part, on its determination that none of these "special circumstances" were implicated by the dual proceedings against the defendant broker-dealer. *See Incendy*, 936 F. Supp. at 956. For further discussion of the *Incendy* decision, see Jennifer D. Antolini, et al., *Securities Fraud*, 34 Am. Crim. L. Rev. 983, 1034 (1997); *see also Farricielli v. State*, No. CV 9605386369, 1997 WL 15405, at *3 (Conn. Super. Jan. 8, 1997).

^{cix} *See id.* (citing *United States v. A Single Family Residence & Real Property Located at 900 Rio Vista Blvd.*, 803 F.2d 625, 629 & n.4 (11th Cir. 1986)). *But see Pervis v. State Farm Fire & Cas. Co.*, 901 F.2d 944 (11th Cir. 1990) (drawing adverse inferences against a party to a civil action when the party declines to testify in his defense constitutes a constitutional violation where the defendant in both a civil and criminal case must "choose" between relinquishing his rights against self-incrimination or foregoing the civil case at the summary judgment stage). As the *Incendy* court recognized, the 11th Circuit's *Pervis* exception is triggered when the invocation of the Fifth Amendment privilege compels automatic summary judgment, not just the loss of the defendant's most formidable defense. *See* 936 F. Supp. at 956 & n.4 (citing *Pervis*, 901 F.2d at 946-47); *see also Arango v. United States Dep't of Treasury*, 115 F.3d 922, 926 & n.10 (11th Cir. 1997).

In *SEC v. Colello*, 139 F.3d 674, 677 (9th Cir. 1998), the SEC brought a securities fraud action against Colello alleging a scheme to defraud whereby a company called Cross Financial Services, Inc. ("CFS") and a number of individuals defrauded more than 700 public investors out of more than \$21 million. The district court granted the SEC's summary judgment and ordered Colello to disgorge \$2,620,598 and pay \$276,954.63 in interest. *Id.* at 675. The district court based its summary judgment for the SEC on Colello's failure to go forward with his defense that he had a legitimate claim to the funds, as well as his resort to the Fifth Amendment. *Id.* at 677. The court explicitly held: "Colello's receipt of investor monies for an alleged purpose

that was never disclosed to the investors, together with his assertion of his Fifth Amendment privilege in response to questions about his ownership claims, demonstrate the absence of any legitimate call on the funds." *SEC v. Cross Fin. Servs., Inc.*, 908 F. Supp. 718, 732 (C.D. Cal. 1995). Colello appealed. The Court of Appeals for the Fourth Circuit affirmed, finding that Colello was free to invoke his Fifth Amendment privilege but that the court was equally free to draw adverse inferences from his failure of proof. 139 F.3d at 677. The court held that even though the Fifth Amendment is violated when refusal to waive the Fifth Amendment privilege leads *automatically* and *without more* to sanctions, a district court does not abuse its discretion when it dismisses a suit after drawing adverse inferences from the assertion of the privilege and after careful review of all the evidence. "the district court also considered the evidence presented by Colello and found nothing in it to support Colello's claims to the funds." *Id.* at 678. The court's dismissal did not turn on Colello's silence alone and was, therefore, not erroneous. *Id.*

^{cx} *Incendy*, 936 F. Supp. at 956.

^{cx} *See SEC v. Rehtorik*, 755 F. Supp. 1018 (S.D. Fla. 1990); *Wehling v. Columbia Broad. Sys.*, 608 F.2d 1084 (5th Cir. 1979). In *Rehtorik*, the court stayed an order of accounting of purportedly fraudulently acquired moneys in a civil action that would have implicated the defendant in a contemporaneous criminal prosecution. *See* 755 F. Supp. at 1019. The court opined that forcing the defendant "to 'speak' in th[e] civil proceeding by ordering an accounting of alleged illicit funds would [have] directly impinge[d] the defendant[s] right against self-incrimination." *Id.* However, the *Rehtorik* court also noted that postponement of an accounting procedure on Fifth Amendment grounds did not preclude the government from seeking summary judgment, nor did it shield the defendant from the adverse inferences drawn from his silence in exercising his Fifth Amendment privilege in the civil case. *See id.* at 1020; *see also Dimensions Med. Ctr., Ltd. v. Principal Fin. Group, Ltd.*, No. 93 C 6264, 1996 WL 494229, at *7 (N.D. Ill. Aug. 21, 1996).

In *Wehling*, the United States Court of Appeals for the Fifth Circuit reversed the district court's dismissal of a libel action in which a plaintiff refused to answer certain questions posed in his oral deposition claiming that disclosure of the requested information could be used against him in a related criminal prosecution. *See* 608 F.2d at 1086. The court noted that the plaintiff did not assert a right to proceed to trial without responding to the questions posed to him in his deposition, but rather, he merely requested the postponement of discovery pending the resolution of the criminal action. *See id.* at 1087. The court explained that "[w]hen plaintiff's silence is constitutionally guaranteed, dismissal is appropriate only where other, less burdensome, remedies would be an ineffective means of preventing unfairness to the defendant." *Id.* at 1088.

Similarly, in *Branaccio v. Mediplex Management of Port St. Lucie, Inc.*, No. 97-1013, 1998 WL 209138 (Fla. App. 4th Dist. Apr. 30, 1998), the court held that a plaintiff's case should not be dismissed: "[w]hen . . . the statute of limitations [had] already run on the [civil] claim, and there is a reasonable foreseeable end in sight for the criminal exposure." In such circumstances "the court in the civil action should ordinarily await that final outcome before addressing whether dismissal is required by unavoidable prejudice to the defendant." 711 So. 2d 1206, 1211-12 (Fla. App. 4th Dist. 1998).

Finally, in *SEC v. Colello*, the court held that "a court has discretion in determining the appropriate means of dealing with a claimant's invocation of the privilege." 139 F.3d at 677 (citing *United States v. \$506,641.00 in United States Currency*, No. 93 C 1603, 1996 WL 78364, at *3 (N.D. Ill. Feb. 20, 1996)).

^{cxii} *See Arden Way Assocs. v. Boesky*, 660 F. Supp. 1494, 1497 (S.D.N.Y. 1987). As the *Arden Way* court admonished, a defendant maintains no constitutional right to a stay of civil proceedings pending the resolution of a factually related criminal proceeding. *See id.* at 1496 (citing *SEC v. Dresser Indus. Inc.*, 628 F.2d 1368, 1375 (D.C. Cir. 1980)). Rather, it is within the inherent discretionary authority of the courts to determine whether a stay is appropriate. *See id.*; *see also Sidari v. Orleans County*, No. 95-250A, 1997 WL 915818, at *2 (W.D.N.Y. May 5, 1997).

In *Cruz v. County of Dupage*, for instance, the court considered the following factors to determine whether the stay should be granted: (1) whether the two actions involve the same subject matter; (2) whether the two actions are brought by the government; (3) the posture of the criminal proceeding; (4) the effect on the public interests at stake if a stay were to be issued; (5) the interest of the plaintiffs in proceeding expeditiously with this litigation and the potential prejudice to plaintiffs of a delay; and (6) the burden that any particular aspect of the proceedings may impose on defendants." No. 96 C 7170, 1997 WL 370194, at *2 (N.D. Ill. June 27, 1997) (citing *Admiral Ins. Co. v. Federal Sec., Inc.*, No. 94 C 5649, 1996 WL 139243 (N.D. Ill. Mar. 26,

1996)); *see also Walsh Sec., Inc. v. Cristo Property Management, Ltd.*, 7 F. Supp. 2d 523, 524 (N.J. 1998); *Gala Enters., Inc. v. Hewlett Packard Co.*, No. 96 CIV. 4864 DC, 1996 WL 732636, at *2 (S.D.N.Y. Dec. 20, 1996).

^{cxiii} *See, e.g., Clark v. United States*, 481 F. Supp. 1086, 1099-1100 (S.D.N.Y. 1979) (discovery delayed); *Corbin v. F.D.I.C.*, 74 F.R.D. 147, 149 (E.D.N.Y. 1977) (deposition stayed).

^{cxiv} *See Fed. R. Civ. P. 30(d)* (1996).

^{cxv} *See, e.g., Dresser*, 628 F.2d at 1375 (noting that courts may postpone discovery, enter protective orders, etc.); *see supra* note 112.

^{cxvi} *See Arden Way*, 660 F. Supp. at 1500.

^{cxvii} *See SEC v. Gruenberg*, 989 F.2d 977, 978 (8th Cir. 1993)(per curiam).

^{cxviii} *See Detroit Police Officers Ass'n v. Young*, 824 F.2d 512 (6th Cir. 1987); *see also In re Bilzerian*, 153 F.3d 1278, 1281 (11th Cir. 1998) (noting that collateral estoppel bars relitigation of an issue if the burden of persuasion in the subsequent proceeding is not significantly heavier).

^{cxix} *SEC v. Monarch Funding Corp.*, 192 F.3d 295, 303 (2d Cir. 1999) (citing *Parklane Hosiery Co. v. Shore*, 439 U.S. 322, 329 (1979)).

^{cxx} *Johnson v. Watkins*, 101 F.3d 792, 795 (2d Cir. 1996)(citation omitted).

^{cxxi} *See Gruenberg*, 989 F.2d at 978 (“It is well established that prior criminal proceedings can work an estoppel in a subsequent civil proceeding, so long as the question involved was ‘distinctly put into issue and directly determined’ in the criminal action.”); *cf. SEC v. Dimensional Entertainment Corp.*, 493 F. Supp. 1270, 1274 (S.D.N.Y. 1980) (holding that material issues resolved against a party in an earlier civil proceeding are binding on that party in subsequent factually related actions initiated by a different opponent); *see also State v. Cedar Park Concrete Corp.*, Nos. 85 CIV. 1887, 86 CIV. 8128, 1997 WL 306909 (S.D.N.Y. Mar. 21, 1997). Moreover, in *SEC v. Monarch Funding Corp.*, the district court noted that “the United States Attorney's Office and the S.E.C. have been considered to be the same party in that both represent the United States.” No. 85 CIV. 7072, 1996 WL 348209, at *3 (S.D.N.Y. June 24, 1996) (quoting *Dimensional Entertainment*, 493 F. Supp. at 1274). It also noted that the application of the doctrine of collateral estoppel does not implicate the Seventh Amendment right to a trial by jury because that right does not attach to SEC’s enforcement proceedings. *See SEC v. Monarch Funding Corp.*, 983 F. Supp. 442, 447 n.7 (S.D.N.Y. 1997), *vacated*, 192 F.3d 295 (2d Cir. 1999).

^{cxxii} 129 F.3d 356 (6th Cir. 1997)(en banc).

^{cxxiii} *Id.* at 360.

^{cxxiv} *Id.* at 362.

^{cxxv} 192 F.3d 295 (2d Cir. 1999).

^{cxxvi} *Id.* at 304.

^{cxxvii} *Id.* at 306.

^{cxxviii} *Id.*

^{cxxix} *Id.*

^{cxxx} *Id.* at 310.

^{cxxxi} See *Fisher v. United States*, 425 U.S. 391, 400-01 (1976) (holding that, for the privilege to apply, there must be testimonial communication, compulsion, and incrimination); see also *United States v. Doe*, 465 U.S. 605, 611-12 (1984); *In re Grand Jury Proceedings Tanager*, 173 F.R.D. 336 (D. Mass. 1997) (where the court held that to sustain the privilege, all that need be shown is that a response is potentially incriminating).

^{cxxxii} See *Leftkowitz v. Turley*, 414 U.S. 70, 77 (1973).

^{cxxxiii} See *United States v. White*, 322 U.S. 694, 699 (1944). See *Water Works & Sewer Bd. of the City of Birmingham v. United States Dept. of Army, Corps of Engineers*, 983 F. Supp. 1052, 1063 & n. 7 (N.D. Ala. 1997) (noting that the privilege against compulsory self-incrimination should be "limited to its historic function of protecting only the natural individual from compulsory incrimination through his own testimony or personal records."), *aff'd*, 162 F.3d 98 (11th Cir. 1998); see also *Central States v. Carstensen Freight Lines, Inc.*, No. 96 C 6252, 1998 WL 413490, at *3 (N.D. Ill. July 17, 1998).

Since *Fisher*, circuit courts have split on whether its rationale extends to private papers, and not just business records, such that there is no Fifth Amendment protection for the contents of any document that was not created under compulsion. The majority view appears to be that the Fifth Amendment does not protect the contents of voluntarily prepared documents, whether business or personal. See, e.g., *Barrett v. Acevedo*, 169 F.3d 1155, 1168 (8th Cir. 1999); *United States v. Grable*, 98 F.3d 251, 253 (6th Cir. 1996), *cert. denied*, 117 S. Ct. 691 (1997); *In re Grand Jury Subpoena Duces Tecum Dated Oct. 29, 1992*, 1 F.3d 87, 93 (2d Cir. 1993); *United States v. Wujkowski*, 929 F.2d 981, 983 (4th Cir. 1991); *In re Sealed Case*, 877 F.2d 83, 84 (D.C. Cir. 1989); *In re Grand Jury Proceedings* on Feb. 4, 1982, 759 F.2d 1418, 1419 (9th Cir. 1985). Several circuits, however, have held that the contents of personal papers remain privileged in certain circumstances. See, e.g., *In re Grand Jury Proceedings*, 55 F.3d 1012, 1013-14 (5th Cir. 1995) (*per curiam*); *In re Grand Jury Proceedings*, 632 F.2d 1033, 1043 (3d Cir. 1980); see also *In re Grand Jury Subpoena Duces Tecum Dated May 9, 1990*, 741 F. Supp. 1059 (S.D.N.Y. 1990), *aff'd*, 956 F.2d 1160 (2d Cir. 1992).

Under *Fisher*, the court must resolve two separate and distinct issues to determine whether personal documents should be accorded protection under the Fifth Amendment: (1) whether the Fifth Amendment protects the contents of the private document, *i.e.*, whether the contents are a *compelled* testimonial and incriminating communication; (2) whether the production of the private document itself has communicative aspects, apart from the contents, which are protected under the Fifth Amendment. See 425 U.S. at 408-10; see also *Barrett v. Acevedo*, 169 F.3d 1155. For an analysis of the second issue, see *United States v. Hubbell*, 120 S.Ct. 2037 (2000); *United States v. Jain*, 152 F.3d 930 (9th Cir. 1998); *United States v. Walker*, 982 F. Supp. 288, 290 (S.D.N.Y. 1997); *Prudential Sec. Inc. v. Brigianos*, 233 A.D.2d 18, 21 (N.Y.A.D. 1st Dept. 1997). In *United States v. Paccione*, 992 F. Supp. 335, 338 (S.D.N.Y. 1998), the court held that the Fifth Amendment shields production of documents if the act of producing them constitutes tacit testimony concerning: (1) the existence of the papers demanded, (2) their possession or control by the witness, or (3) the witness' belief that the papers are those described in the subpoena. Also, discussing whether defendant could claim the Fifth Amendment Privilege to refuse to produce documents subpoenaed by the SEC, the Second Circuit held that "production of documents in response to a subpoena may not be refused if the government can demonstrate with reasonable particularity that it knows of the existence and location of the documents." *SEC v. Waltzer & Assocs.*, No. 96-6261, 1997 WL 561062, at *3 (2d Cir. Sept. 10, 1997) (internal citation omitted). The court noted that while communicative, the production under these circumstances was not incriminatory. *Id.*

^{cxxxiv} See *Hale v. Henkel*, 201 U.S. 43, 75 (1906). See *Water Works & Sewer Bd. of the City of Birmingham v. United States Dept. of Army, Corps of Engineers*, 983 F. Supp. at 1063 & n.7; see also *United States v. Maxey & Co., P.C.*, 956 F. Supp. 823, 827 (N.D. Ind. 1997); *Central States v. Carstensen Freight Lines, Inc.*, 1998 WL 413490, at *3.

^{cxxxv} See *Braswell v. United States*, 487 U.S. 99, 113 (1988). See *SEC v. Oxford Capital Sec., Inc.*, 794 F. Supp. 104, 107-08 (S.D.N.Y. 1992) (corporations cannot refuse to provide documents required for accounting in securities action on grounds production would violate its officers' Fifth Amendment privilege against self-incrimination.)

In *United States v. McLaughlin*, 126 F.3d 130, 133 (3d Cir. 1997), *cert. denied*, 118 S. Ct. 2366 (1998), defendant was convicted of tax evasion. Defendant appealed contending that the trial court violated his Fifth Amendment privilege in admitting the government's use at trial of evidence intending to show intentional tax evasion by defendant. The Court of Appeals for the Third Circuit held that even though a corporate custodian produces documents in his representative rather than his personal capacity and, therefore, may not invoke his right against self-incrimination in order to resist a subpoena for corporate records, he nevertheless can claim his Fifth Amendment privilege as to the act of disclosure itself. The court held that, in this case, "[t]he government's repeated reference to Russell's incomplete act of production as evidence of his culpability flies in the face of *Braswell* and vitiated Russell's Fifth Amendment privilege." *Id.*; *see also SEC v. Bremont*, No. 96 CIV. 8771 (LAK), 1997 WL 225803, at *1 (S.D.N.Y. May 6, 1997).

cxvvi *See United States v. Dean*, 989 F.2d 1205, 1210 (D.C. Cir. 1993).

cxvii *See White*, 322 U.S. at 701.

cxviii *See Bellis v. United States*, 417 U.S. 85, 95 (1974).

cxvix *See Fed. R. Evid.* 801(a)(2).

cxl *See Griffin v. California*, 380 U.S. 609, 615 (1965). The test for determining whether an indirect remark constitutes an improper comment on a defendant's failure to testify is: "Was the language used manifestly intended to be, or was it of such character that the jury would naturally and necessarily take it to be a comment on the failure of the accused to testify." *United States v. Whitehead*, 618 F.2d 523, 527 (4th Cir. 1980); *see also United States v. McCormick*, 972 F.2d 343, 1992 WL 189499, at *2 (4th Cir. 1992).

cxli 425 U.S. 308 (1976); *see also Libutti v. United States*, 107 F.3d 110, 121 (2d Cir. 1997).

cxlii *Baxter*, 425 U.S. at 318.

cxliii *See id.* at 317-18.

cxliv *See supra* Parts XXII and XXIII.

cxlv Civil Action No. 96-2192 (NHJ) (D.C. Cir. Dec. 20, 1996).

cxlvi *Id.* at 2-3.

cxlvii 425 U.S. at 318.

cxlviii *See Linde Thomson Langworthy Kohn & Van Dyke, P.C. v. R.T.C.*, 5 F.3d 1508, 1513 (D.C. Cir. 1993).

cxlix *Baxter*, 425 U.S. at 319.

cl *See Griffin v. California*, 380 U.S. 609 (1965).

cli 55 F.3d 78 (2d Cir. 1995); *see also Centennial Life Ins. Co. v. Nappi*, 956 F. Supp. 222, 228 (N.D.N.Y. 1997). *See generally supra* note 131.

clii *Id.* at 84.

cliii *Id.*

cliv *Id.* at 85. *See, e.g., Phillip Morris Inc. v. Heinrich*, No. 95 CIV 0328 (LMM), 1998 WL 167333, at *1-*2 (S.D.N.Y. Apr. 8, 1998).

^{clv} *Id.* at 84.

^{clvi} 25 F.3d 187 (3d Cir. 1994). In *United States v. Ehrlich*, No. CIV. A. 95-661, 1998 WL 372355, at *6 (E.D. Pa. May 28, 1998), the court citing *SEC v. Graystone Nash., Inc.* stated "(t)he decision to invoke or waive the Fifth Amendment is not always self-evident, and it requires serious consideration of the consequences. Counseling by a lawyer familiar with the ramifications of a particular case and the intricacies of the law in this area is highly desirable." *Id.* (citing *SEC v. Graystone Nash., Inc.*, 25 F.3d at 192-93.)

^{clvii} *SEC v. Graystone Nash., Inc.*, 25 F.3d at 192.

^{clviii} *See id.* at 193.

^{clix} *Id.* at 194.

^{clx} *See, e.g., In re Edmond*, 934 F.2d 1304, 1308-09 (4th Cir. 1991); *United States v. Parcels of Land*, 903 F.2d 36, 42-46 (1st Cir. 1990); *see also Bourgal v. Robco Contracting Enters., Ltd.*, 969 F. Supp. 854, 861 (E.D.N.Y. 1997).

^{clxi} 958 F. Supp. 846 (S.D.N.Y. 1997), *aff'd*, 159 F.3d 1348 (2d Cir. 1998).

^{clxii} *See Wolfe v. United States*, 291 U.S. 7, 14 (1934); *see also Blau v. United States*, 340 U.S. 332, 333 (1951) ("[M]arital communications are presumptively confidential."); *United States v. Rakes*, 136 F.3d 1, 3 (1st Cir. 1998).

^{clxiii} *Wolfe*, 291 U.S. at 14. The *Wolfe* court emphasized the significance of confidentiality with regard to the marital communications privilege. *See id.* at 14-15. The Court explained that while communications between husband and wife are presumptively confidential, "when made in the presence of a third party, such communications are usually regarded as not privileged because [they were] not made in confidence." *Id.* at 14. *Wolfe* dealt with the admissibility of a statement contained in a letter written by the petitioner to his wife proven not by the testimony of either spouse, but by the testimony of a stenographer who had dictated and transcribed the letter. *See id.* at 12. The petitioner argued that just as the privilege with respect to communications between an attorney-client and doctor-patient extends to third party intermediaries (*e.g.*, nurses, secretaries, clerks), so too, does the privilege accorded private spousal communications encompass communications made in the presence or aid of a third party "whose duties, in common experience, are confidential." *Id.* at 15. The *Wolfe* Court disagreed, maintaining that unlike physician-patient or attorney-client communications, "[n]ormally husband and wife may conveniently communicate without stenographic aid and the privilege of holding their confidences immune from proof in court may be reasonably enjoyed without embracing within it the testimony of third persons to whom such communications have been voluntarily revealed." *Id.* at 16-17. Moreover, the Court opined that the marital communications privilege "suppresses relevant testimony and should be allowed *only* when it is plain that marital confidence can not otherwise reasonably be preserved." *Id.* at 17 (emphasis added).

^{clxiv} *See Pereira v. United States*, 347 U.S. 1, 6-7 (1954); *Blau*, 340 U.S. at 333; *Wolfe*, 291 U.S. at 14; *see also United States v. Evans*, 966 F.2d 398, 401 (8th Cir. 1992) (explaining that the marital communications privilege "extends only to words or acts that are intended as a communication to the other spouse"). However, the privilege does not preclude disclosure of actions observed by a spouse. *See Abbott v. Kidder, Peabody & Co.*, No. 97 C 3251, 1997 WL 337228, at *4 (N.D. Ill. June 16, 1997); *SEC v. Cavanagh*, 1 F. Supp. 2d 337, 361 (S.D.N.Y. 1998); *SEC v. Cavanagh*, No. 98 CIV. 1818, 1998 WL 440029, at *3 (S.D.N.Y. July 27, 1998); *see also Preserving the Marital Communications Privilege in Subpoena Enforcement Proceedings*, 66 Geo. Wash. L. Rev. 988 (1998).

^{clxv} *See Pereira*, 347 U.S. at 6 (noting that a divorce does not terminate the privilege for confidential marital communications); *see also Evans*, 966 F.2d at 401 ("The communication must... also occur during a time when the marriage is valid under state law and the couple is not permanently separated.").

clxvi *See id.*

clxvii *See S.E.C. v. Lavin*, 111 F.3d 921, 925 (D.C. Cir. 1997).

clxviii 111 F.3d 921 (D.C. Cir. 1997).

clxix Evidence of the trader's diligent efforts to protect the privacy of conversations with his spouse was important in light of the *Lavin* court's admonition that "the confidentiality of communications covered by a privilege must be jealously guarded by the holder lest it be waived." 111 F.3d at 929 (quoting *In re Sealed Case*, 877 F.2d 976, 980 (D.C. Cir. 1989)). The Court explained that adherence to a strict rule on waiver of privileges advances the public interest "by encouraging full and frank communications within special relationships." *Id.* (internal citations omitted).

clxx *See id.* at 930. The *Lavin* court relied upon *United States v. de la Jara*, 973 F.2d 746 (9th Cir. 1992). In *de la Jara*, police officers executing a search warrant seized a letter to the appellant from his attorney that purportedly evinced their participation in a continuing criminal or fraudulent activity. *See* 978 F.2d at 748. At trial six months later, the appellant challenged the admissibility of the letter on the ground of attorney-client privilege. *See id.* The Ninth Circuit held that the appellant waived the attorney-client privilege with respect to the letter by failing to assert it in a timely manner. *See id.* at 749-50. Because "[the appellant] did nothing to recover the letter or protect its confidentiality during the six-month interlude between its seizure and introduction into evidence," the *de la Jara* court explained, "he allowed the mantle of confidentiality which once protected the document to be irretrievably breached." *Id.* at 750 (internal quotations and citations omitted). Relying on the Ninth Circuit's rationale in *de la Jara*, the *Lavin* court reasoned that the standard applied to compelled disclosures by law enforcement officials of otherwise privileged communications is also germane in circumstances "where a party had no real control over the disclosure or nondisclosure of documents." 111 F.3d at 930.

clxxi *Aramony v. United Way of Am.*, 969 F. Supp. 226, 235 (S.D.N.Y. 1997). Generally, if a party voluntarily discloses a privileged document, it waives any claim of privilege and cannot later seek to keep the document confidential. *See id.*

clxxii *See, e.g., United States v. Gangi*, 1 F. Supp.2d 256, 264 (S.D.N.Y. 1998); *Aramony*, 969 F. Supp. at 235; *Lois Sportswear, U.S.A., Inc. v. Levi Strauss & Co.*, 104 F.R.D. 103, 105 (S.D.N.Y. 1985).

¹⁷³ 189 F.R.D. 83 (S.D.N.Y. 1999).

clxxiv *Id.* at 85 n.4.

clxxv *Id.* at 86.

clxxvi *Id.*

clxxvii *Id.*

clxxviii *See id.*

clxxix 15 U.S.C. § 78u(c); *see also*, § 209(c) of the Investment Advisers Act of 1940, 15 U.S.C. § 80b-9(c); § 42(c) of the Investment Company Act of 1940, 15 U.S.C. § 80a-41(c); § 18(d) of the Public Utility Holding Companies Act of 1935, 15 U.S.C. § 79r(d); § 19(b) of the Securities Act, 15 U.S.C. § 77s(b); § 321 (a) of the Trust Indenture Act of 1939, 15 U.S.C. § 77u(a).

clxxx *See supra* Part XVIII.

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- clxxxi *SEC v. Financial Inst. Assurance Corp.*, [1985-1986 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 92,212 (N.D. Ga. 1985).
- clxxxii Section 21(c) of the Exchange Act, 15 U.S.C. § 78u(c); § 209(c) of the Investment Advisers Act of 1940, 15 U.S.C. § 80b-9(c); § 42(c) of the Investment Company Act of 1940, 15 U.S.C. § 80a-41(c); § 18(d) of the Public Utility Holding Companies Act of 1935, 15 U.S.C. § 79r(d).
- clxxxiii *Penfield Co. v. SEC*, 330 U.S. 585, 593 (1947).
- clxxxiv *Nilva v. United States*, 352 U.S. 385 (1957); *Beebe v. Auslander*, 629 F.2d 985 (4th Cir. 1980).
- clxxxv *Reisman*, 375 U.S. at 449.
- clxxxvi *Maggio v. Zeitz*, 333 U.S. 56 (1948); *SEC v. Ormont Drug & Chem. Co.*, 739 F.2d 654 (D.C. Cir. 1984).
- clxxxvii *In re Marc Rich & Co., A.G.*, 736 F.2d 864 (2d Cir. 1984).
- clxxxviii 15 U.S.C. § 78u(c).
- clxxxix *United States v. Smith*, SEC Lit. Release No. 4078 (S.D.N.Y. 1968); *SEC v. Lord*, 24 SEC Ann. Rep. 54 (S.D.N.Y. 1958).
- exc A bona fide contention will not result in punishment under this provision. *Guaranty Underwriters v. Johnson*, 133 F.2d 54 (5th Cir. 1943).
- exc i 17 C.F.R. § 202.5(b).
- exc ii 17 C.F.R. § 202.5(d).
- exc iii 17 C.F.R. § 202.5(c).
- exc iv Securities Act Release No. 5310 (Sept. 27, 1972), Fed. Sec. L. Rep. (CCH) ¶ 4995.
- exc v *SEC v. National Student Marketing Corp.*, 538 F.2d 404, 407 (D.C. Cir. 1976) (per curiam).
- exc vi *Wellman v. Dickinson*, 79 F.R.D. 341, 348 (S.D.N.Y. 1978).
- exc vii 17 C.F.R. § 202.5(c).
- exc viii *See, e.g.*, 17 C.F.R. § 203.7(a).
- exc ix *Procedure Relating to the Commencement of Enforcement Proceedings and Termination of Staff Proceedings*, Securities Act Release No. 5310, 2 Fed. Sec. L. Rep. (CCH) ¶ 4995, at 4319 (Sept. 27, 1972).
- ec 762 F. Supp. 604 (S.D.N.Y. 1991), *motion to alter and amend denied*, No. 88 CIV. 8587 (CSH), 1991 WL 275760 (S.D.N.Y. Dec. 19, 1991).
- cci 5 U.S.C. § 552(a)(1)(D).
- ccii 17 C.F.R. § 200.80(a)(1)(IV).
- cciii 5 U.S.C. § 552(a)(2)(B).
- cciv 5 U.S.C. § 552(a)(1)(D).

^{ccv} See *Mada-Luna v. Fitzpatrick*, 813 F.2d 1006, 1012-13 (9th Cir. 1987).

^{ccvi} 17 C.F.R. § 203 *et seq.*

^{ccvii} 5 U.S.C. § 552(a)(2)(B).

^{ccviii} 17 C.F.R. § 202.5(c).

^{ccix} *Procedure Relating to the Commencement of Enforcement Proceedings and Termination of Staff Investigations*, Securities and Exchange Act Release No. 34-9796, 1972 WL 18218 (S.E.C.), at *2 (Sept. 27, 1972).

^{ccx} Release No. APR-293, 1988 WL 357006 (S.E.C.), at *2 (Mar. 21, 1988).

^{ccxi} Release No. APR-194, 1977 WL 23921 (S.E.C.), at *3 (June 14, 1977).

^{ccxii} Release No. APR-511, 1996 WL 325248 (S.E.C.), at *1 n.2 (June 3, 1996).

^{ccxiii} *Cf. SEC v. Sloan*, 436 U.S. 103 (1978); *United States v. Brown*, 79 F.3d 1550, 1562 (11th Cir. 1996).

^{ccxiv} This section is reprinted from an article that first appeared in 5 Securities Reform Act Litigation Reporter 792 (August 1998).

^{ccxv} 87 F.3d 484 (D.C. Cir. 1996).

^{ccxvi} Section 2462 provides in relevant part that "an action, suit or proceeding for the enforcement of any civil fine, penalty, or forfeiture, pecuniary or otherwise, shall not be entertained unless commenced within five years from the date when the claim first accrued...." 28 U.S.C. § 2462 (1998). Section 2462 provides a "catch-all" statute of limitations where Congress does not expressly include a statutory time limitation. See *Federal Election Comm'n v. National Republican Senatorial Comm.*, 877 F. Supp. 15, 17 (D.D.C. 1995).

^{ccxvii} On several occasions the United States Supreme Court has struggled to define "penalty" within the meaning of the Constitution. See, e.g., *Austin v. United States*, 509 U.S. 602, 621-22 (1993) (concluding that because civil forfeiture pursuant to 21 U.S.C. §§ 881 (a)(4) & (a)(7) does not serve solely a remedial purpose, but also to punish and deter, the forfeiture constitutes punishment or a penalty within the meaning of the Eighth Amendment). *But see Bennis v. Michigan*, 516 U.S. 442, 448 (1996) (apparently suggesting that because civil forfeiture of an innocent owner's property at least partially serves a deterrent purpose distinct and separate from any punitive purpose, the forfeiture does not constitute a punishment or penalty sufficient to trigger the due process protections provided under the Fourteenth Amendment). In *United States v. Halper*, 490 U.S. 435, 448-49 (1989), the Supreme Court held that a civil sanction constitutes a penalty or punishment within the meaning of the Double Jeopardy Clause when the "sanction cannot fairly be said solely to serve a remedial purpose, but rather can only be explained as also serving either retributive or deterrent purposes" *Halper* was abrogated by *Hudson v. United States*, 118 S. Ct. 488 (1997). *Halper's* abrogation calls into question whether *Johnson* would be decided in the same way today, at least with respect to its penalty analysis.

^{ccxviii} See *Johnson*, 87 F.3d at 492. In *Johnson*, the D.C. Circuit extended the rationale established in *3M Co. v. Browner*, 17 F.3d 1453, 1463 (D.C. Cir. 1994). In *3M*, the court held that section 2462's five-year statute of limitations applies not only to judicial proceedings, but also to administrative proceedings. See *id.* at 1457. Specifically, the *3M* court held that section 2462 barred the imposition of civil penalties for violations of the Toxic Substances Control Act. See *id.* at 1463. Other courts have followed *3M* in considering the applicability of section 2462 in the context of various administrative proceedings. See, e.g., *United States v. Banks*, 115 F.3d 916, 919 (11th Cir. 1997), *cert. denied*, 118 S. Ct. 852 (1998) (violations of the Clean Water Act); *Interamericas Invs., Ltd. v. Board of Governors*, 111 F.3d 376, 382 (5th Cir. 1997) (violations of the Bank Holding Company Act); *Arch Mineral Corp. v. Babbitt*, 104 F.3d 660, 670 (4th Cir. 1997) (violations of the Surface Mining Control and

Reclamation Act); *Federal Election Comm'n v. Williams*, 104 F.3d 237, 239-40 (9th Cir. 1996) (violations of the Federal Election Campaign Act), *cert. denied*, 118 S. Ct. 600 (1997); *Johnson*, 87 F.3d at 492 (holding that section 2462 applies to S.E.C. proceedings that seek to censure and suspend a securities supervisor).

^{ccxix} See Harry Weis & Laura Walker, *The Impact of Johnson v. S.E.C.: The S.E.C. Grapples with the Punitive Effects of a Suspension*, 981 PLI/Corp. 23, 25 (1997).

^{ccxx} 681 F. Supp. 1 (D.D.C. 1987).

^{ccxxi} 15 U.S.C. § 78u *et seq.*

^{ccxxii} 750 F. Supp. 14 (D.D.C. 1990).

^{ccxxiii} 689 F. Supp. 767 (S.D. Ohio 1988).

^{ccxxiv} *Id.*; see also *SEC v. Warner*, 652 F. Supp. 647 (S.D. Fla. 1987).

^{ccxxv} 5 U.S.C. § 552 (1998); see also *Chilivis v. SEC*, 673 F.2d 1205, 1210-11 (11th Cir. 1982).

^{ccxxvi} See *Parker/Hunter, Inc. v. SEC*, (1981 Transfer Binder), Fed. Sec. L. Rep. (CCH) ¶ 97, 873 (D.D.C. 1981).

^{ccxxvii} 17 C.F.R. § 200.80(b)(7)(i)(A) (1998).

^{ccxxviii} See *Jos. Schlitz Brewing Co. v. SEC*, 548 F. Supp. 6 (D.D.C. 1982).

^{ccxxix} 441 U.S. 281 (1979).

^{ccxxx} 17 C.F.R. § 200.83(g)(1) (1998).

^{ccxxxi} 17 C.F.R. § 200.83(d)(2)(iii) (1998).

^{ccxxxii} 17 C.F.R. § 200.83(d)(2)(iii) (1998).

^{ccxxxiii} 17 C.F.R. § 200.83(d)(2)(iv)-(v) (1998).

^{ccxxxiv} 17 C.F.R. § 200.83(d)(2)(vi) (1998).

^{ccxxxv} 17 C.F.R. § 200.83(d)(2)(vii) (1998).

^{ccxxxvi} 17 C.F.R. § 200-83(d)(2)(viii) (1998).

^{ccxxxvii} 17 C.F.R. § 200.83(e) (1998).

^{ccxxxviii} 17 C.F.R. § 200.83(e)(5) (1998).

^{ccxxxix} 17 C.F.R. § 200.83(h) (1998).

^{ccxl} 17 C.F.R. § 200.80(b)(4) (1998).

^{ccxli} *Chilivis v. SEC*, 673 F.2d 1205, 1211 (11th Cir. 1982).

^{ccxlii} *Consumers Union of United States, Inc. v. Veterans Admin.*, 301 F. Supp. 796, 801 (S.D.N.Y. 1969).

ccxliii *House Comm. on Gov't Operations, Clarifying and Protecting the Right of Public Information*, H.R. Rep. No. 1497, 89th Cong., 2d Sess. 10 (1966).

ccxliv 498 F.2d 765 (D.C. Cir. 1974).

ccxlv *Kissinger v. Reporters Comm. for Freedom of Press*, 445 U.S. 136, 152 (1980).

ccxlvi *Id.* at 151.

ccxlvii *Id.*

ccxlviii The foregoing section on the Freedom of Information Act was adopted from an article by Frank C. Razzano and Lawrence D. Schlang entitled "*FOIA and SEC Inquiries*," which appeared in *1 J. Corp. Disclosure & Confidentiality*, 23 *et seq.* (September 1989). The reader is referred to that article for other possible arguments and means of protecting records produced to the SEC during an investigation.

ccxlix 12 U.S.C. § 3401 *et seq.* (1998).

cccl 12 U.S.C. § 3404 (1998).

cccli 12 U.S.C. § 3405 (1998).

ccclii 12 U.S.C. § 3410(a) (1998).

cccliii *Id.*

cccliv *Id.*

ccclv 12 U.S.C. § 3410(c) (1998).

ccclvi 15 U.S.C. § 78u(h)(2) (1997).

ccclvii *Hunt v. SEC*, 520 F. Supp. 580 (N.D. Tex. 1981).

ccclviii *In re United States Securities and Exchange Commission Private Investigation/Application of John Doe re: Certain Subpoenas*, (1990 Trial Binder) Fed. Sec. L. Rep. (CCH) ¶ 95,424 (S.D.N.Y. 1990); *see also Mackey v. SEC*, Nos. 3:96MC407 (AHN), 3:96MC415 (AHN), 1997 WL 114801, at *3 (D. Conn. 1997), *see supra* note 42.