ALM | LAW.COM

New York Law Journal

What to Expect in the Securities Enforcement Space in 2025

By Lisa Bebchick, Helen Gugel, Amish Shah and Dominique Rioux

December 13, 2024

Securities enforcement is not going anywhere in 2025. The enforcement agenda of the Securities and Exchange Commission (SEC) will surely be impacted by its new leadership under Paul Atkins, President-elect Donald Trump's selection for SEC chair and a former SEC commissioner from 2002 to 2008. But the agency's core commitments—policing fraud and market manipulation, perceived conflicts of interest, and conduct that may harm retail investors—have historically been championed by commissioners of both parties and are likely to continue unabated. Even in areas in which enforcement is likely to substantially diminish—such as crypto or environmental, social, and governance (ESG) disclosures—the SEC will likely still have interest when there are concrete allegations of fraud or investor harm. One notable change, however, is that the SEC may be less likely to support enforcement based on technical violations of the federal securities laws that lack intentionality or specific underlying harm. New leadership might also implement procedural changes that will affect how investigated parties and their counsel experience the enforcement process, and we may see a substantial reduction in penalties against public companies, given that Atkins has criticized such penalties as harming existing shareholders. Finally, there is uncertainty regarding staffing at the SEC that may impact SEC enforcement in the coming years.

U.S. Securities and Exchange Commission building in Washington, D.C.

Substantive Priorities—What Will Change and What Will Remain the Same?

- **Diminished crypto-related enforcement actions but a continued focus on fraud**

The SEC's scrutiny of the crypto industry—and the articulation of its broad view that digital assets are securities subject to the agency's jurisdiction—began during Trump's first term under the leadership of former Chair Jay Clayton. Over the last four years, however,

President-elect Trump has become a vocal supporter of crypto, and his nomination of Paul Atkins for SEC chair suggests that the SEC's focus on the crypto industry will relax significantly in 2025. Under Chair Gary Gensler, there has been a substantial increase in the number and reach of crypto-related enforcement actions and a willingness to bring cases against well-established exchanges and other market participants based on the SEC's determination that they are listing or otherwise transacting in securities. This approach has been heavily criticized as "regulation by enforcement" by proponents of the industry and, perhaps more critically, by Atkins and the two current Republican SEC commissioners (one of whom will also serve as acting chair until a permanent chair is appointed). For instance, Commissioners Hester Peirce and Mark Uyeda have repeatedly criticized the agency for failing to provide clear guidance about when digital assets are considered a security, thereby stifling innovation and creating an untenable environment for market participants in this space. (See Peirce & Uyeda, "On Today's Episode of As the Crypto World Turns: Statement on ShapeShift AG" (March 5, 2024)). Atkins has similarly expressed concerns that the SEC's approach to crypto enforcement has driven innovation abroad, harming U.S. interests. (See Dave Michaels, "Trump Picks Paul Atkins to Run SEC," Wall Street Journal (Dec. 4, 2024)).

While we expect that the SEC will take a less aggressive approach to crypto enforcement going forward and bring fewer cases for an alleged failure to register with the agency in connection with transactions involving digital assets, the SEC is not likely to step back from crypto enforcement entirely. As Commissioner Peirce has said, "focusing on crypto, which has been plagued by fraud, is not inherently problematic." (See Peirce, "Hobs and Hobbes: Wharton FinTech Lecture" (Nov. 1, 2024); see also Peirce, "Overdue: Statement of Dissent on LBRY" (Oct. 27, 2023)). Crypto cases that implicate fraud or retail investor harm are likely to be a continuing priority.

- **Potential for increased AI-related enforcement and anti-ESG enforcement**

The SEC has long prioritized enforcement actions for false or misleading statements, disclosures, or marketing materials. The SEC recently extended these cases to cover "AI-washing," which is when companies, investment advisers, or other regulated entities overstate the extent to which they are using artificial intelligence (AI) as part of their business. Enforcement actions focused on AI-washing are likely to continue in 2025, as they squarely fit within the SEC's traditional enforcement of false and misleading statements.

For the same reason, we expect the SEC to continue to bring enforcement actions that allege misstatements related to ESG. Beyond that, however, we anticipate that other ESG-related enforcement actions will continue to be deprioritized, as they have been towards the end of the Biden administration. It is possible that the Commission might even advance new, potentially opposing policy priorities in 2025, whether anti-ESG, anti-DEI, or other policy preferences of the incoming Trump Administration. (See, e.g., "Agenda47: President Trump Continues to Lead on Protecting Americans from Radical Leftist ESG Investments", Trump Campaign Website (Feb. 25, 2023); Gram Slattery & Nathan Layne, "Trump vows to fight 'anti-white feeling' in the United States," Reuters (May 4, 2024)). For instance, the commission could adopt a position similar to that of Republican Attorneys General who have argued, among other things, that ESG is antithetical to funds' fiduciary duty to maximize returns. (See "Letter from 21 Attorneys General to Asset Managers" (March 30, 2023)). Indeed, Atkins has expressed the view that ESG funds are politicized investment products and that activism through investment can harm investors by leading "fund managers to compromise their fiduciary duty in service of a political agenda." (See Paul Atkins, "Opinion: Activist Investment Puts Millions of Retirees at Risk," Newsweek (March 6, 2023)).

- **A renewed focus on traditional enforcement theories**

Under Gensler, the SEC advanced novel legal theories that have pushed the boundaries of securities enforcement. Some of these theories were successful, such as the SEC's recent trial victory in

the *Panuwat* "shadow trading" case. In that case, the SEC brought an insider trading action against an individual who—in contravention of his employer's insider trading policy—used nonpublic information about his employer to purchase call options in a different, comparable company. (See SEC Director of Enforcement Gurbir S. Grewal, "Statement on Jury's Verdict in Trial of Matthew Panuwat" (April 5, 2024)). Other novel theories have failed, such as the recent SolarWinds litigation in which the SEC attempted to argue that the cybersecurity deficiencies at SolarWinds that resulted in the SUNBURST cyberattack (discovered in December 2020) violated Section 13(b)(2)(B) of the Exchange Act, which requires public companies to "devise and maintain a system of internal accounting controls sufficient to provide reasonable assurances that … access to assets is permitted only in accordance with management's general or specific authorization." (See *Securities & Exchange Commission v. SolarWinds*, No. 23-civ-9518 (PAE) (S.D.N.Y. July 18, 2024)). The court rejected the SEC's broad reading of Section 13(b)(2)(B) to cover areas unrelated to financial accounting or transactions, explaining that the SEC's reading of the statute would grant the agency authority to regulate "all systems public companies use to safeguard valuable assets," whether the selection of padlocks, background checks for security guards, or the length of passwords—an expansion of the SEC's authority that Congress clearly did not intend.

We expect that the SEC under the Trump administration will be less inclined to aggressively pursue novel legal theories, particularly given the Republican commissioners' emphasis on predictability and avoiding regulation by enforcement. Instead, we anticipate seeing a focus on the more traditional SEC priorities that have been bipartisan: financial and offering fraud, fiduciary duty and conflicts of interest disclosure, well-established insider trading theories, revenue recognition and other accounting control violations, the Foreign Corrupt Practices Act (FCPA), and straightforward violations of SEC rules.

- **Decline in technical rule violation cases where there is no intentional wrongdoing or specific underlying harm**

As part of its aggressive enforcement agenda under Gensler, the SEC brought many cases alleging only technical rule violations without any indicia of intentional wrongdoing or specific underlying harm. The most notable category of these cases is the SEC's off-channel communications sweep, which aggressively policed registered entities' compliance with the record keeping requirements of the federal securities laws. Since launching the initiative in December 2021, the SEC has charged over 100 firms and collected over $2 billion in penalties. Going forward, we anticipate that the SEC will not pursue off-channel communications actions that are purely technical violations and instead will likely prioritize only those cases in which there are significant and extensive record keeping failures—such as those where there was a "widespread failure" that was "firmwide," "not hidden," and impacted the commission's ability to carry out its responsibilities. (See Peirce & Uyeda, "A Catalyst: Statement on Qatalyst Partners LP," (Sept. 24, 2024)). Commissioners Peirce and Uyeda have also signaled an openness to modifying and modernizing the record keeping rules to better align with the realities of today's technology.

We may also see a decline in other technical rule violation cases. For example, the SEC recently announced actions against 23 entities and individuals to enforce the deadlines of various reporting requirements of Sections 13 and 16 of the Exchange Act. Some of these actions covered filings that were years old or merely two weeks late. It is unclear if the SEC under new leadership would support such enforcement actions absent evidence of specific underlying harm or other aggravating factors, such as the insider or company being a serial offender.

Potential Procedural Changes

With new leadership, we can also expect some shifts in the SEC's enforcement procedures in 2025. One possible change concerns the exchange of information between the SEC and the potential target of an enforcement action, known as the "Wells Process." If, following an investigation, the SEC is prepared to recommend an enforcement action to

the commission, the Enforcement staff will typically notify the prospective defendant in a "Wells notice." Defense counsel subsequently makes a Wells submission and requests a meeting with staff to explain why the respondent should not be charged. In recent years, the SEC has taken steps to limit the number of Wells meetings conducted at the end of an investigation and reduce the frequency of director-level participation in Wells meetings, affording more deference to the staff attorneys closest to the investigation. (See SEC Director of Enforcement Gurbir S. Grewal, "Remarks at SEC Speaks 2021" (Oct. 13, 2021); SEC Deputy Director of Enforcement Sanjay Wadhwa, "Remarks at SEC Speaks" (Sept. 9, 2022)). A new Director of Enforcement may be more willing to take Wells meetings and engage in more dialogue with counsel at the end of an investigation.

The existing deference to SEC staff in other areas could also change under new leadership. For instance, the Commission may insist on substantive review of formal orders authorizing Enforcement staff to issue subpoenas (or may require such review for particular types of cases). The Commission might also require more senior officials to take part in settlement discussions. Such developments may result in more protracted investigations or reduce the overall number of investigations that are initiated. We will also likely see changes to the Enforcement Division's approach to remedies. For instance, the Enforcement Division under the prior Trump administration imposed less severe penalties than under the previous and subsequent administrations. Indeed, as a former commissioner, Atkins criticized large penalties against public companies, arguing that such penalties further victimize shareholders who were already harmed by a company's wrongdoing. We might also see the SEC requiring more limited undertakings in settlement agreements.

Uncertainty Regarding SEC Staffing

We have already seen turnover recently at senior levels in the Enforcement Division. Presidential transitions are frequently a time for higher volumes of staff departures from federal agencies and this trend can be expected to continue in 2025. There is a question about how the SEC will handle this expected attrition given its current hiring freeze. At least in the near term, reductions in staff will necessarily require the Enforcement Division to be even more selective about the investigations it prioritizes and to focus on more traditional priorities.

President-elect Trump has also signaled that he will implement the policy described in his October 2020 "Schedule F" executive order. Before being reversed by President Joe Biden, that executive order stripped civil service protections from a number of career federal employees that had positions of a "confidential, policy-determining, policymaking, or policy-advocating character." If Trump successfully implements Schedule F, the extent of the impact on SEC personnel is unclear but has the potential to further reduce the SEC's staffing levels and affect substantive priorities.

Conclusion

It is important to remember that while change will come with any new administration, the bulk of an agency's work will remain largely unaltered. We expect that historical precedent to hold true for the SEC in 2025. It also remains to be seen how long it will take for any of the Commission's new agenda shifts to take hold. Practitioners and registered entities are well served by continuing to adhere to the SEC's current rules and guidance as they keep a close eye on leadership and priority changes as they unfold.

Lisa Bebchick *is a partner in Ropes & Gray's litigation and enforcement practice group.* **Helen Gugel** *is a partner in the firm's New York office.* **Amish Shah** *is counsel in the firm's Washington, D.C. office and* **Dominique Rioux** *is an associate in the Boston office of the firm.*