
SEC Reverses Policy on Conditional Settlement Offers

On February 11, 2021, the Acting Chair of the U.S. Securities and Exchange Commission (“SEC” or “Commission”), Allison Herren Lee, announced that the Division of Enforcement will no longer recommend to the Commission settlement offers conditioned upon waivers of certain automatic disqualifications that arise following violations of federal securities laws.¹ The announcement marks a return to the Commission’s long-standing, prior practice of segregating the waiver application process from settlement negotiations. This practice was briefly abandoned beginning in July 2019 when then-SEC Chairman Jay Clayton announced that settling parties may submit settlement offers conditioned upon waivers from disqualification.²

I. Background

Certain violations of the federal securities laws may trigger automatic disqualification from exercising privileges granted under the securities laws. For example, an individual or entity with a criminal conviction involving a securities law violation or that faces a securities industry bar may lose the ability to serve as an investment advisor or underwriter for an investment company pursuant to Section 9(a) of the Investment Company Act of 1940.³ In addition, a party that violates federal securities laws may lose the ability to rely on exemptions under Regulations D, A, and Crowdfunding under the Securities Act of 1933 (“Securities Act”).⁴ And, the offending party may no longer be entitled to take advantage of the statutory safe harbor for forward looking statements and may lose status as a Well-Known Seasoned Issuer (“WKSII”) under Rule 405 of the Securities Act.⁵

In the face of such collateral consequences, individuals and entities negotiating a settlement with the SEC often will seek from the Commission a waiver of any automatic disqualification that could be triggered by the potential settlement. Waiver requests usually are sought contemporaneously with settlement offers so that, upon entry of settlement, the settling parties’ operations are not adversely affected. Historically, the Commission’s Divisions of Corporation Finance and Investment Management has reviewed waiver applications, while the Division of Enforcement separately handled settlement negotiations.

In July 2019, then-Chairman Jay Clayton began permitting a settling entity to request that the Commission consider offers of settlement that “simultaneously addresses both the underlying enforcement action and any related

¹ Allison Herren Lee, *Statement of Acting Chair Allison Herren Lee on Contingent Settlement Offers* (Feb. 11, 2021), available at <https://www.sec.gov/news/public-statement/lee-statement-contingent-settlement-offers-021121>.

² Jay Clayton, *Statement Regarding Offers of Settlement* (Jul. 3, 2019), available at <https://www.sec.gov/news/public-statement/clayton-statement-regarding-offers-settlement>.

³ 15 U.S.C. § 80a-9(a).

⁴ 17 C.F.R. § 230.506; 17 C.F.R. § 230.504; 17 C.F.R. § 230.262; 17 C.F.R. § 227.100 et seq.

⁵ 15 U.S.C. § 77z-2; 15 U.S.C. § 78u-5; 17 C.F.R. § 230.405.

collateral disqualifications.”⁶ Under this approach, the Commission could consider offers of settlement conditioned upon the grant of a forward-looking waiver. The stated rationale for this policy change was to reduce potentially protracted settlement negotiations. Then-Chairman Clayton emphasized that keeping settlement offers and waiver applications separate resulted in a process that was formulaic and overly complex and ignored the reality that the two events are always interconnected.

II. Policy Reversal and Response

On February 11, 2021, Commissioner Lee, who was designated Acting Chair of the Commission by President Biden on January 21, 2021, reversed the July 2019 policy change and reverted to the Commission’s historical practice regarding the consideration of waivers. She explained the need to “reinforce the critical separation between the Commission’s enforcement process and its consideration of requests for waivers from automatic disqualifications that arise from certain violations or sanctions.”⁷ Acting Chair Lee emphasized that segregating settlement offers from waiver applications will eliminate the potential for “structural conflicts or pressures” that arise during the settlement negotiation process, such as the use of waivers as bargaining chips to induce a settlement or giving the appearance that the Commission will issue waivers automatically.⁸

Following the announcement, Commissioners Hester Peirce and Elad Roisman issued a joint statement criticizing the policy reversal. They explained that the new policy “marks a return to an unwieldy process that treats as completely separate what is in fact interrelated. It re-introduces an artificial separation between the process by which an entity reaches a resolution on its violations of securities laws and the process by which it obtains clarity with respect to the collateral consequences of those violations.”⁹ Commissioners Peirce and Roisman expressed concern that the policy reversal will bring about a delay in the prompt resolution of unlawful conduct and introduce uncertainty for the settling parties as to whether a waiver will be granted.

III. Implications

The Commission’s recent policy reversal may impact the willingness of individuals and entities to settle with the Commission. Parties considering settlement will need to grapple with the uncertainty that a settlement agreement may not guarantee a waiver from certain collateral consequences. The settlement process also could become more protracted as settling parties will need to take additional steps to ensure what they view to be adequate protections from unforeseen consequences of a potential settlement. In addition, the Commission’s approach may signal a harsher stance toward waivers in general under the Biden Administration.

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⁶ Jay Clayton, *Statement Regarding Offers of Settlement* (Jul. 3, 2019), available at <https://www.sec.gov/news/public-statement/clayton-statement-regarding-offers-settlement>.

⁷ Allison Herren Lee, *Statement of Acting Chair Allison Herren Lee on Contingent Settlement Offers* (Feb. 11, 2021), available at <https://www.sec.gov/news/public-statement/lee-statement-contingent-settlement-offers-021121>.

⁸ *Id.*

⁹ Hester M. Peirce and Elad L. Roisman, *Statement of Commissioners Hester M. Peirce and Elad L. Roisman on Contingent Settlement Offers* (Feb. 12, 2021), available at <https://www.sec.gov/news/public-statement/peirce-roisman-statement-contingent-settlement-offers-021221>.

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