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### **A Questionable Delegation of Authority: Did the SEC Go Too Far When It Delegated Authority to the Division of Enforcement to Initiate an Investigation?**

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**A seemingly innocuous decision by the Commission may have had a tremendous impact on the SEC's Enforcement Program. In 2009, under Chairman Mary Shapiro, the Commissioners of the Securities and Exchange Commission delegated authority to the Director of Enforcement to open formal orders of investigation of persons and entities. The Director then sub-delegated authority to Regional Directors, Associate Directors, and Specialized Unit Chiefs. A formal order of investigation is the precursor to the SEC Staff issuing subpoenas for documents and testimony.** Prior to the delegation of authority, the Division of Enforcement was required to present reasons to the Commission for the request for a formal order, and the Commission would vote, often in a summary fashion, to grant or deny the formal order. The rationale for delegating formal order authority was that the Commission rarely declined to issue the formal order. In fact, some statistics suggested that the Commission approved almost 99% of the requests by the Staff to issue a formal order of investigation. Of course, whatever the approval rate, the fact that the Commission needed to approve a formal order provided an important internal check to prevent abuse. In other words, the very fact that approval was required may have prevented the Staff from pursuing questionable investigations.

The delegation of formal authority has raised three concerns.

**First, the fact that formal orders (and thus subpoenas) can be obtained now with relative ease – an SEC Enforcement Staff lawyer simply can request a formal order from his or her ultimate supervisor – has resulted in the Staff resorting to subpoenas earlier in the enforcement investigative process.** Under the prior system, the Enforcement Staff often would call the entity under investigation and engage in informal detective work prior to resorting to a request from the Commission for a formal order. That informal detective work benefited the Staff by allowing the Staff to forgo a more elaborate investigation when the initial, informal steps gave assurances there was no wrongdoing. Companies benefited by avoiding the costly production of thousands or millions of documents in response to an SEC subpoena by instead engaging in an initial conversation and voluntary production of key documents to demonstrate there was no violation. Now, under delegated authority, the Staff does not need to exercise those informal investigative steps, resorting instead to the resource-intensive subpoena for documents that often consumes Enforcement Staff resources for several months and, in some instances, unnecessarily.

The **second concern** with delegated authority is that it eliminated a process whereby the Commission can be involved in enforcement cases at the early stages. **Without the authority**



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**to issue formal orders, the Commission now rarely is briefed on any particular enforcement action until the late stages when the Staff seeks to bring charges.** The Commission does not have the visibility to provide guidance to the Enforcement Staff prior to the case unfolding. The Staff is free to pursue any investigation no matter how resource-intensive to the SEC or costly to an individual or entity, without Commissioners even being aware. Moreover, under the prior system, the Commissioners would know precisely the suspicions that prompted the initial formal order and could measure those suspicions against the final enforcement recommendation, which might differ substantially. In other words, the Commissioners might find it informative whether a multi-year investigation into the initial issues yielded no enforcement action on those concerns but instead resulted in an enforcement action concerning entirely different issues.

The **third concern** with delegated authority is the balkanization of investigative authority. Under the prior system, the fact of an investigation would be raised to the highest levels of the Commission – to both the Director and the Commission – and would be known to anyone in the Division of Enforcement who wished to attend the closed Commission meeting where the matter was discussed. This centralization enabled a Staff member in a regional office to see areas that were being investigated by a different regional office. Moreover, senior officers in the Division of Enforcement could offer assistance to others in the Division upon hearing about a new investigation. The system enabled greater flow of communication and cooperation. **Under the new delegated authority, a formal order of investigation could be opened by one regional office without others in the Division even knowing at the time.**

**The Commission should re-evaluate whether it should continue with its delegation of authority to initiate formal investigations. The authority to initiate an investigation is a power that might best reside with the five Commissioners.**

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