

## E-ALERT | White Collar

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### SEC DOLES OUT MINIMAL BENEFIT TO COOPERATOR

Since the enactment of Dodd-Frank, there has been a great deal of focus on rewards for “whistleblowing”— bringing to the government’s attention evidence of wrongdoing that it did not previously know about. Yet a much more common question is how much credit to give wrongdoers who are first approached by investigators, but who could still help them make a fast, easy case against others, if the government made it worth their while. In a recent insider trading action, *SEC v. Wrangell*, the SEC announced that it had rewarded this type of cooperator, but the amount of the reward appears inadequate to induce widespread cooperation.

The cooperator, Kenneth Wrangell, allegedly was a second-tier tippee who made approximately \$42,500 from trading on nonpublic information about an impending merger.<sup>1</sup> When contacted by SEC staff, the SEC said, Mr. Wrangell promptly “provided truthful details acknowledging his own trading and entered into a cooperation agreement that resulted in direct evidence being quickly developed against [the inside source of the information and his direct tippee].”<sup>2</sup> The Commission characterized his cooperation as “significant” and “extensive,” and said it enabled the agency “to swiftly reach settlements with all three individuals to recover ill-gotten monetary gains.”<sup>3</sup>

What was Mr. Wrangell’s reward? The SEC charged him with a Section 10(b) violation and alleged that he “will continue” to engage in securities fraud unless the court orders him to stop.<sup>4</sup> He was required to consent to a permanent injunction, disgorge his trading profits plus interest, and pay a penalty. The SEC then issued a press release naming him and further publicizing his alleged wrongdoing. The only benefit he received, according to the SEC, was a reduction of his penalty to \$11,380. Assuming he would have otherwise paid the standard “one time” penalty equal to his alleged trading profits, as did the corporate board member who divulged the confidential information at issue, Mr. Wrangell’s cooperation saved him about \$31,000. Perversely, Mr. Wrangell could even end up paying a larger penalty than the non-cooperating direct tippee, since the SEC’s settlement with him provides that the amount of his monetary sanctions will be determined by the court.

Mr. Wrangell’s reward was at the low end of the scale set out in the SEC’s January 2010 cooperation policy, which states that rewards for cooperating individuals can range from no enforcement action to reduced charges and sanctions.<sup>5</sup> While a modestly reduced penalty was evidently enough for Mr. Wrangell, it does not seem sufficient to incentivize broad cooperation. The stated goal of the SEC’s

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<sup>1</sup> See “SEC Charges Three in North Carolina With Insider Trading,” SEC Press Release No. 2012-193 (Sept. 20, 2012), available at <http://www.sec.gov/news/press/2012/2012-193.htm>.

<sup>2</sup> *Id.*

<sup>3</sup> *Id.*

<sup>4</sup> Complaint ¶5, in *SEC v. Wrangell* (E.D.N.C., filed Sept. 20, 2012), available at <http://www.sec.gov/litigation/complaints/2012/comp-pr2012-193-wrangell.pdf>.

<sup>5</sup> *Policy Statement of the Securities and Exchange Commission Concerning Cooperation by Individuals in its Investigations and Related Enforcement Actions*, 17 C.F.R. § 202.12, quoted in the SEC Division of Enforcement’s Enforcement Manual § 6.1.1, available at <http://www.sec.gov/divisions/enforce/enforcementmanual.pdf>.

cooperation policy is to maximize its “law enforcement interests.”<sup>6</sup> In our view, the SEC would better achieve this goal by conferring additional benefits on cooperators like Mr. Wrangell, such as eliminating penalties entirely, forgoing injunctions, and/or charging them with non-scienter-based violations or as relief defendants. Even with more generous benefits to cooperators in run-of-the-mill cases such as this one, the SEC still could reserve its most valuable reward—taking no enforcement action at all against the cooperator—for substantial cooperation in its most significant and highest priority cases, as it did on one occasion earlier this year.<sup>7</sup>

In view of the SEC’s stingy approach to rewarding cooperation by individuals, and the relative paucity of guidance provided by the SEC on how it is applying its cooperation policy in specific cases, potential cooperators should carefully consider the likely benefits and costs of cooperation.

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If you have any questions concerning the material discussed in this client alert, please contact the following members of our white collar practice group:

<b>Bruce Baird</b>	202.662.5122	<a href="mailto:bbaird@cov.com">bbaird@cov.com</a>
<b>David Kornblau</b>	212.841.1084	<a href="mailto:dkornblau@cov.com">dkornblau@cov.com</a>
<b>Alan Vinegrad</b>	212.841.1022	<a href="mailto:avinegrad@cov.com">avinegrad@cov.com</a>

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<sup>6</sup> *Id.*

<sup>7</sup> See “SEC Credits Former Axa Rosenberg Executive for Substantial Cooperation during Investigation,” SEC Litigation Release No. 22298 (Mar. 19, 2012), available at <http://www.sec.gov/litigation/litreleases/2012/lr22298.htm>; “Commission Credits Individual Under Cooperation Initiative,” Public Statement by Robert Khuzami, Director, SEC Division of Enforcement, available at <http://www.sec.gov/news/speech/2012/spch031912rk.htm>.