Proskauer

SEC Rule 15a-6 Enforcement

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Last week the Securities and Exchange Commission ("SEC") charged four India-based financial services firms for providing brokerage services to U.S. institutional investors without operating under a 15a-6 chaperoning agreement or registering as a broker-dealer. The four firms paid more than $1.8 million combined to settle the SEC's charges. The SEC said it is continuing to look for potential violations at other firms. These actions may signal greater SEC scrutiny of foreign firms' U.S. brokerage activities.

Absent an applicable exception or exemption, Section 15(a) of the Securities Exchange Act of 1934 ("Exchange Act") generally prohibits a broker or dealer from making use of the mails or any means or instrumentality of interstate commerce (the "jurisdictional means") to effect any transactions in, or to induce or attempt to induce the purchase or sale of, any security without being registered with the SEC as a broker-dealer.

Section 3(a)(4) of the Exchange Act defines a "broker" as any person (other than a person meeting the conditions of an exception, exemption or safe harbor, such as an associated person of an issuer meeting the conditions of the "Issuer Exemption" under Rule 3a4-1 or a bank meeting the conditions of Regulation R) engaged in the business of effecting transactions in securities for the accounts of others.

Rule 15a-6 under the Exchange Act provides conditional exemptions from broker-dealer registration under which, among other things, unregistered foreign broker-dealers may effect transactions with or for U.S. institutional investors and major institutional investors in certain limited circumstances. Inducing or attempting to induce securities transactions constitutes solicitation requiring broker-dealer registration. Solicitation is construed broadly to include both efforts to induce a single transaction and efforts to develop an ongoing securities business relationship.

According to the SEC's orders, the four unregistered foreign firms engaged with U.S. investors in the following impermissible activities:

- sponsored conferences in the U.S.,

their employees traveled regularly to the U.S. to meet with investors,

- traded securities of India-based issuers on behalf of U.S. investors, and
- participated in securities offerings from India-based issuers to U.S. investors.

As a result of their conduct, the SEC concluded that each of the four firms "willfully violated" Section 15(a) of the Exchange Act. Importantly, however, the SEC noted that a willful violation of the securities laws means merely that the person charged knows what he is doing – there is no requirement that he also be aware he is violating the securities laws.

Each of the firms agreed to be censured and to pay disgorgement and prejudgment interest. The firms' cooperation with the SEC staff and their prompt remedial measures, either entering into a 15a-6 chaperoning agreement or initiating broker-dealer registration, were cited as important factors in accepting their settlement offers and the SEC's decision not to impose cease-and-desist orders or penalties.

These cases may presage a trend toward more vigorous enforcement of the broker-dealer registration requirements for foreign financial firms engaging in brokerage activities with U.S. institutional investors, even where violations are not deliberate.

Despite the growing interaction between foreign firms and U.S. institutions, there was little enforcement action around Rule 15a-6 before 2008. In the CentreInvest case that year, however, the SEC charged that 000 CentreInvest Securities, a Moscow-based unregistered broker-dealer, directly and through its New York affiliate, CentreInvest, Inc., and other persons working for the Moscow and New York firms, solicited institutional investors in the U.S. to purchase thinly-traded stocks of Russian companies without registering as a broker-dealer or meeting the requirements for exemption from registration for foreign broker-dealers under Rule 15a-6. Among other things, the SEC concluded that the Moscow broker had an undisclosed control relationship with the New York affiliate and that both firms knew their operations did not meet the requirements of Rule 15a-6.

The SEC described the violations in the CentreInvest case as serious and recurrent and involving the deliberate disregard of regulatory violations. In 2009, an Administrative Law Judge granted the SEC Enforcement Division's motion and imposed a cease-and-desist on the unregistered Moscow broker, barred it from association with any broker-dealer, ordered it to disgorge all gains from its activities as an unregistered broker and required it to pay civil monetary penalties.

While the CentreInvest case signaled the SEC's intention to address deliberate violations of Rule 15a-6, these new cases, coupled with the SEC's statement that it is continuing to look for potential violations at other firms, suggest a broader enforcement focus with respect to Rule 15a-6. Unlike the CentreInvest case, there is no suggestion in these recent cases that any of the firms involved deliberately disregarded the broker-dealer registration requirements. Irrespective of intentionality, the SEC warns that foreign broker-dealers must educate themselves on U.S. laws and regulations when they provide services to U.S. investors.