

KIRKLAND ALERT

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Insider Trading Investigations: Initial Response to Subpoenas and Search Warrants

In the last week, news of search warrants and subpoenas for records relating to suspected insider trading has dominated the headlines. According to news reports, including in the *Wall Street Journal*, the SEC and U.S. Attorney's Office for the Southern District of New York, working with the FBI, have been conducting insider-trading investigations into securities trading by hedge funds, mutual funds and other financial institutions, and more investigations are underway. Although these investigations include scrutiny of the roles of consultants and subject-matter experts retained by financial firms ostensibly for market-intelligence, they are notable for their scope, reaching deeply into the financial services industry and seeking broad categories of records in an apparent effort to piece together insider trading cases from a variety of sources of potential evidence.

With broad and intensive insider-trading investigations sweeping through the industry, it would be prudent for financial institutions to have an action plan in place in the event they are swept within the investigative net, either as a third-party witness asked to provide documents and records, or as subjects or targets of an investigation. Experience has shown that how a financial institution responds within the first 48 hours of receiving a subpoena can often have a critical impact on the investigation's outcome. Below, we discuss the questions that typically arise when a financial firm receives a subpoena, and considerations that inform what to do in the first 48 hours of receiving one.

What does receiving a subpoena mean? The SEC's Enforcement Division conducts investigations pursuant to formal Orders of Investigation that authorize the Division staff to demand the production of relevant information, either in the form of documents or witness testimony. Although the SEC itself has civil — and not criminal — enforcement power, the SEC can and does refer cases for criminal investigation to the U.S. Attorney's Office. The U.S. Attorney's Office typically works with the F.B.I. and a federal grand jury — which is empowered to compel the production of documents and/or the appearance of witnesses for testimony — to investigate criminal violations. Note that the SEC and U.S. Attorney's Office often coordinate their investigations. Thus, receiving an SEC subpoena does not necessarily mean that the investigation is only civil in nature. Other agencies, such as state Attorney General's Offices and District Attorneys Offices, also have subpoena power. Other points to keep in mind:

- The government often issues document subpoenas before seeking to interview or subpoena witnesses. Document subpoenas can be directed at entities or individuals that the government believes may have information that is relevant to the investigation. After reviewing the documents, the government may well subpoena additional documents or witnesses for testimony.
- Absent agreement with the government or a court order to the contrary, compliance with both SEC and grand jury subpoenas is mandatory. Oftentimes, counsel can negotiate limitations to the scope of the subpoena and/or extensions of time for compliance. In certain cases, when a subpoena is overbroad or unduly burdensome and no compromise can be reached, the recipient can seek relief in court through a "motion to quash" the subpoena. Such motions are rarely granted and should be brought only after careful consideration.

- The recipient of a federal grand jury subpoena is entitled to be told whether it is a mere “witness” in the investigation (and not suspected of wrongdoing), a “subject” (viewed as having possible involvement in wrongdoing), or a “target” (affirmatively suspected of wrongdoing). Counsel for your firm can have this discussion with the responsible Assistant U.S. Attorney. Note, however, that these designations can change as the investigation unfolds.
- Unlike the U.S. Attorney’s Office, the SEC is not required to — and typically does not — disclose, the investigative status of the subpoena recipient.
- There is also no obligation on the SEC or the U.S. Attorney’s Office to describe the nature of the investigation. Counsel for your firm may engage in a dialogue with the government to gain further insight into the issues at hand.

What is the obligation to preserve documents? A party receiving a subpoena (or who reasonably anticipates that it will come under investigation) has a legal obligation to preserve potentially relevant materials.

- If you receive a subpoena, you must take reasonable steps to preserve potentially relevant hard-copy documents, as well as e-mails and other electronically stored information. This includes suspending document retention policies and the automated deletion of emails. Other steps may also be necessary, depending on the circumstances.
- You should also issue a properly drafted written legal hold notice, and actively manage the preservation process. Individual employees who receive subpoenas are obligated to preserve not only work-related materials, but also personal materials, even if kept outside of the office, including in the home.
- The intentional destruction of potentially relevant documents is a crime, and can result in prosecution even if there is no underlying insider-trading or other violation.
- Even the inadvertent destruction of documents may generate greater investigative scrutiny than

the underlying conduct, and, depending on the circumstances, can result in civil fines and sanctions.

What if the subpoena is overbroad and burdensome? Often a subpoena requests a large volume of information that must be produced in a matter of days or weeks.

- Counsel should contact the SEC staff or Assistant U.S. Attorney to acknowledge receipt of the subpoena and to start a dialogue between your organization and the government.
- Counsel may have an opportunity to discuss the scope of the subpoena, the priority of the information to be produced, and any deadlines. This type of dialogue may help streamline and prioritize your response.
- Even if you think the subpoena is overbroad, it is prudent promptly to take steps to preserve potentially relevant information.
- As noted, if an agreement cannot be reached to limit the scope, recipients have recourse to the courts to seek to “quash” or “modify” an unreasonable subpoena. However, the government has wide latitude to subpoena information and such motions succeed only in rare cases.

Should I talk to the SEC or U.S. Attorney’s Office directly? Generally, counsel handles communications with the government.

- It is a crime to knowingly mislead a federal agent about a material matter, even during a casual phone conversation, and regardless of whether you have been placed under oath. The government may view even innocent inaccuracies with skepticism and investigate to determine if intentional obstruction was involved.
- Once the government learns that a party is represented by counsel, it may not contact that party directly, but must go through counsel. Note, however, that simply because a firm is represented by counsel does not necessarily mean that all of its individual employees are also represented.

- The government is also generally free to contact *former* employees and other third-parties directly until such time as they are represented by their own counsel.
- Counsel for individuals frequently advise employees concerning their Fifth Amendment rights against self-incrimination, and whether asserting those rights is in their best interests.

Should employees discuss the investigation among themselves? The short answer is “no more than absolutely necessary.” Aside from cooperating with firm counsel, employees should be discouraged from engaging in informal or unnecessary discussion of the subpoena or investigation among themselves.

- Informal communications about the subpoena among employees may be subject to scrutiny during the investigative process. Ill-conceived emails relating to the subpoena or the investigation can be taken out of context and can create unnecessary problems.
- If employees later testify, they may be required to disclose with whom they spoke and what was said. Such discussions can be perceived negatively as an improper effort to “get their stories straight.”

What if the FBI arrives at our office with a search warrant? If the FBI arrives at your offices or home with a search warrant, that means that the government has already convinced a judge that there is “probable cause” to believe that evidence of a criminal violation is located there.

- Do not obstruct or impede the search; alert your counsel to the search.
- Counsel can arrive on the scene, examine the search warrant, help keep track of what is taken, and otherwise assist you in responding appropriately to the search warrant.

Conclusion

Kirkland has an extensive team of experienced white-collar defense attorneys ready to assist in responding to SEC subpoenas, grand jury subpoenas, search warrants and investigations. If an investigation cannot be resolved, our team is experienced in defending against enforcement actions and criminal charges in all phases, including at trial. We are happy to address any further questions you may have.

If you have any questions about the matters addressed in this *Kirkland Alert*, please contact the following Kirkland authors or your regular Kirkland contact.

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