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Loss Contingencies: Recent Enforcement Action Shows Need for Good Faith Assessment

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John Sample, Ghillaine Reid, and Jay Dubow's recent article "[SEC Digs in on Loss Contingency Disclosure Requirements](#)" was quoted in *TheCorporateCounsel.net's* article "[Loss Contingencies: Recent Enforcement Action Shows Need for Good Faith Assessment](#)."

Between January and May 2018, defendants — the former CEO, the former CFO, and a former director of the Company — allegedly violated federal securities laws when they made false and misleading statements to outside auditors about an ongoing SEC investigation into the Company's investment in a biotechnology company (the Biotech Investment). Despite knowing of the investigation and the SEC's intention to recommend charging the Company with violating federal securities laws, the defendants told the auditors that they were not aware of "any situations where the company may not be in compliance with any federal or state laws or government or other regulatory body regulations."

The veracity of this assertion was rendered false once it was discovered that, between March 2015 and November 2018, the SEC's Division of Enforcement sent multiple subpoenas to the Company, its officers, and directors, requesting documents and seeking testimony related to the SEC's investigation into the Biotech Investment. Moreover, in April 2017, the SEC's Division of Enforcement sent a Wells notice to the Company notifying it of the SEC staff's intention to recommend charges.

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Situations like the above are not isolated events. In today's ecosystem, companies are more likely than ever to be faced with the potential for investigation or other enforcement action by any number of regulatory bodies — whether it be the SEC, FINRA, NASDAQ, DOJ, FTC, OSHA, and so on. In the face of such investigations or enforcement actions, companies often struggle with assessing when events have escalated such that they are subject to disclosure requirements. This assessment can be difficult, therefore it is crucial that companies undertake a diligent review and engage appropriate assistance to ensure the accuracy and rigor of that review.

Indeed, as noted by the SEC in its order, "...[the Company and its officers] never conducted a good faith assessment as to whether the possible pending enforcement action needed to be disclosed. Instead, the Company and its officers did the opposite — they mislead [the Company's] auditors and failed to disclose the existence and status of the SEC's [] investigation." Casting a blind eye will not aid in the avoidance scrutiny, but rather will heighten the degree of attention focused on each and every deficiency.

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