Analysis

SEC's Cooperman Deal Gives Defense Bar New Tool

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Law360, New York (May 19, 2017, 8:43 PM EDT) -- Billionaire hedge fund founder Leon Cooperman and his firm Omega Advisors Inc. managed to avoid an industry bar in settling the U.S. Securities and Exchange Commission's insider trading claims, and experts say their unusual compromise of retaining a compliance consultant gives the defense bar ammunition for negotiating future deals.

Although the SEC reportedly sought to suspend Cooperman from the securities industry for a period of time in settlement talks before it first brought the case last September, the agency ultimately agreed to let the trader and his firm go for a **$4.9 million fine** and no suspension.

Instead, the settlement included an agreement requiring Cooperman and Omega to retain an independent compliance consultant who will review their trading and recommend improvements, a deal experts said is out of the ordinary and will inspire defense attorneys to seek similar relief in their own insider trading cases.

"It serves as a benchmark," David Chase of the Law Firm of David R. Chase said of the compliance consultant. "The SEC can't be held to it, but certainly the securities defense bar will remind it the next time there's a case that's similar."

The SEC had alleged in its September complaint that Cooperman used his status as a major shareholder of Atlas

Pipeline Partners to get information about the company's 2010 sale of an operating facility from an executive, who passed it along with the expectation that Cooperman would not trade on it.

Cooperman, however, allegedly used the information to purchase Atlas securities ahead of the $682 million asset sale. The sale, once announced, caused Atlas' shares to jump more than 31 percent and increased the value of other related securities, the SEC said.

In addition to the insider trading charges, Cooperman was also accused of violating the SEC's beneficial ownership rules — which require individuals or entities that own more than 5 percent or 10 percent stakes in public companies to disclose their holdings and transactions.

The SEC said Cooperman flouted those rules regularly and repeatedly, either failing to make the requisite disclosures or delaying making the disclosures on more than 40 instances across eight companies.

Cooperman and Omega settled the case without admitting or denying the findings. The manager and his firm will jointly be responsible for paying $2.2 million in disgorgement and interest and a $1.7 million penalty for the insider trading violations, while Cooperman is on the hook for an additional $1 million penalty to settle the beneficial ownership reporting claims.

But the aspect of the settlement getting the most attention is the requirement that Cooperman and Omega retain an onsite independent compliance consultant for the next five years, who will be able to access any electronic communications and trading records without prior notice.

The consultant will be responsible for reviewing trades by Cooperman and Omega, recommending improvements and conducting training at the firm, and reporting to the SEC. Cooperman and his fund will also have to make monthly certifications that their trades were not based on material nonpublic information in violation of the Exchange Act.

The SEC uses compliance consultants and monitors frequently in some types of cases, particularly in settlements of Foreign Corrupt Practices Act violations, but the consultants are rarely included in insider trading deals.

The last notable use was the agency's requirement that SAC Capital Advisors LP manager Steven A. Cohen retain an independent consultant to conduct reviews of his so-called family office, Point72 Asset Management LP — but even in that case, **the settlement** barred Cohen from supervising funds that manage outside money until the end of 2017.

The SEC characterized the Cooperman settlement as a victory on Thursday. Acting Enforcement Director Stephanie Avakian issued a statement saying the deal would protect against future violations while requiring significant fines.

"By imposing an independent consultant to monitor their trading activity, the resolution helps protect our markets from future risk of insider trading," Avakian said.

Attorneys for Cooperman and Omega also framed the deal as a win. Dan Kramer and Ted Wells of Paul Weiss Rifkind Wharton & Garrison LLP issued a statement Thursday saying "we and our client are very pleased with this outcome, which speaks for itself."

In some ways, the deal is "a classic compromise," Fenwick & West LLP partner Michael S. Dicke said, where both sides felt there was risk to litigating and wanted to cut a deal that enabled the agency to impose a prophylactic measure as close as possible to a suspension while Cooperman escaped a potentially career-killing bar.

Steve Crimmins, a partner at Murphy & McGonigle PC and a former SEC enforcement attorney, said the consultant proposed by the settlement is a "very, very aggressive and comprehensive program" that imposes

significant requirements on Cooperman and Omega and gives the consultant broad powers.

The agreement likely required "a lot of good lawyering on both sides of the matter," Crimmins said, as the SEC and Cooperman's attorneys at Paul Weiss and Ballard Spahr LLP hammered out the details.

"It's a very unique remedy that's crafted to deal with a very unique situation," Crimmins said.

But experts also noted the unusual settlement is a significant departure from the temporary industry bar the SEC was reportedly demanding earlier in the litigation.

"What jumps out at me is that there's no suspension and time out of the industry," Chase said.

Chase, a former SEC prosecutor, said the agency could have been persuaded to take a more lenient stance to avoid a Third Circuit appeal over potentially thorny issues of insider trading law.

Cooperman had sought permission to **file an interlocutory appeal** in April, after a Pennsylvania federal judge **rebuffed his argument** that he couldn't be held liable under the misappropriation theory of insider trading because he only agreed not to trade on a tip, giving rise to a duty of trust and confidence, after he received the information.

U.S. District Judge Juan R. Sánchez acknowledged that whether liability under the misappropriation theory could be premised on a post-disclosure agreement was a "novel issue" that has not been addressed by other courts.

But he sided with the SEC, finding the theory only requires a duty of trust to exist when the recipient trades on the information, meaning trades Cooperman made after the agreement constituted insider trades.

Although the SEC prevailed on the issue at the district court, Dicke said the uncertainty surrounding Cooperman's request for an interlocutory appeal on the insider trading issue could have pushed both the fund manager and the SEC to negotiate the settlement.

"The reason I think that both sides looked at this and decided it was a good case to compromise was the legal issue was novel," said Dicke, who previously served as the associate regional director for enforcement in the SEC's San Francisco office.

The SEC may have been especially concerned that taking the case to the Third Circuit could set a bad enforcement policy if the appellate court reversed the district court decision, Chase said, possibly giving Cooperman's counsel more leverage to cut a better deal.

"The SEC's very sensitive about trying to avoid bad decisions that could create bad precedents," Chase said. "That very well could have been a critical factor in driving the settlement."

The fact that the agency sought an industry bar under former Chair Mary Jo White but ultimately settled for the independent monitor under new Chairman Jay Clayton was also not lost on observers, although experts said it's likely too early to tell whether Clayton's SEC will be more lenient in other cases as well.

Chase said the change could be an early signal that the cost of settling an enforcement action has gone down under the Trump Administration and Clayton's leadership.

"It could be an indication of a sea change in terms of the remedies that the SEC is going to be willing to consider to resolve a case," he said. But he added it could also be a one-off deal.

Crimmins said it's possible that SEC staff will employ compliance consultants more often in cases going forward, but more likely they'll only use the remedy to deal with unique situations. He noted that it does set a

precedent by creating a new approach to resolve cases when the situation warrants.

In this instance, Crimmins said, the SEC may also have taken a more lenient approach after considering the impact barring Cooperman would have on Omega's investors.

The lack of a ban "probably reflects the staff's feeling that Cooperman's continuous involvement in the business is necessary for his own investors and potentially for the companies that his fund has invested in," Crimmins said.

While the settlement won't be precedential, defense attorneys will no doubt seek to argue the same relief is appropriate in similar situations where an industry bar could harm a firm and its investors, Dicke said.

"Where I could see its real utility coming up is when you have a small trading firm that depends on a single individual and where a bar would essentially cause that business to have to shut down," Dicke said. "I could imagine there being a push to substitute a monitor for a complete bar."

Attorneys may not stop at small, owner-run firms. Chase said that, whether or not the SEC is eager to substitute compliance consultants for industry bars going forward, it certainly already knows that securities defense lawyers will be looking for similar deals in other insider trading actions.

"I will tell you that the next time I have an insider trading case at the SEC, like any other defense counsel, we're going to point to this case and say, 'We want that deal or a form of that deal,'" Chase said.

The SEC is represented by Bridget M. Fitzpatrick, Jennifer Chun Barry, Mark R. Sylvester, Oreste P. McClung, Brendan P. McGlynn and Christopher R. Kelly.

Cooperman is represented by Daniel J. Kramer, Theodore V. Wells Jr., Gregory F. Laufer and Richard C. Tarlowe of Paul Weiss Rifkind Wharton & Garrison LLP and Henry E. Hockeimer Jr. and Timothy M. Stengel of Ballard Spahr LLP.

The case is Securities and Exchange Commission v. Leon G. Cooperman and Omega Advisors Inc., case number 2:16-cv-05043, in the U.S. District Court for the Eastern District of Pennsylvania.

--Additional reporting by Kat Greene and Jack Newsham. Editing by Philip Shea and Kelly Duncan.