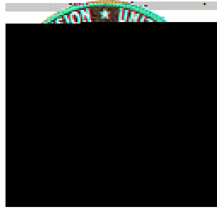
United States of America
FEDERAL TRADE COMMISSION
Washington, D.C. 20580



Office of Commissioner
Rohit Chopra

MEMORANDUM 2018-01

TO: Commission Staff and Commissioners

FROM: Commissioner Rohit ChopT0 1 Tf 11.04 3.0 S-6w2 0 Td (4d6-6w)5(2 0 Td0s)]TJD1--ra5

Federal law enforcement and regulatory agencies should vigorously enforce their orders, which have the force of law. While the FTC has undertaken a number of initiatives to stop recidivism, such as Project Scofflaw in 1996, there have been instances where other agencies have been more equivocal about their commitment to keeping wrongdoers on the right side of the law.

When companies violate orders, this is usually the result of serious management dysfunction, a calculated risk that the payoff of skirting t

spot market.[2] The law requires that these companies be automatically disqualified from preferential access to capital markets. However, the Securities and Exchange Commission has issued waivers – over and over again – to these institutions, allowing them to continue their preferential access in spite of serial violations of the law.[3]

The automatic disqualifications were designed, in part, to serve as a strong deterrent to engaging in misconduct. But with these repeated waivers, institutions will not factor this consequence into their risk-reward calculations.

This is not the only recent example of a perception of lax enforcement. After HSBC admitted its involvement in a massive money laundering scheme involving Colombian and Mexican drug cartels, regulators opted to settle the case with a deferred prosecution agreement[4] – even though this was the third time in ten years that the bank had been cited for weak controls.[5] No bank executives were prosecuted.

Demanding structural remedies is rare, and often comes too late. Over the last three years, for example, Wells Fargo has been accused of opening accounts without customer authorization,[6] illegally repossessing service members' cars,[7] charging customers for unneeded auto insurance,[8]

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[2] Press Release, U.S. Dep't of Justice, Five Major Banks Agree to Parent-Level Guilty Pleas (May 20, 2018), https://www.justice.gov/opa/pr/five-major-banks-agree-parent-level-guilty-pleas. One of the financial institutions was also found to have violated a non-prosecution agreement related to LIBOR manipulation.

[3] See Dissenting Statement of U.S. Sec. and Exch. Commissioner Kara M. Stein Concerning Certain Waivers Granted by the Commission for Certain Entities Pleading Guilty to Criminal Charges Involving Manipulation of Foreign Exchange Rates (May 21, 2015), https://www.sec.gov/n

and hitting homeowners with improper fees,[9] among other charges. The breadth of the alleged misconduct may have been a problem of skewed incentives, or it may have been a symptom of the board's and management's inability to adequately oversee the megabank's sprawling businesses, or both.

Noting "pervasive and serious compliance and conduct failures[,]" the Federal Reserve Board of Governors eventually ordered the company to restrict its growth, and accused its lead independent director of "ineffective oversight."[10] The Office of the Comptroller of the Currency took action as well, vetting the appointment of new executives and directors, and reserving the right to seek dismissal of top leaders.[11] It is likely that if this type of relief had been pursued earlier, the company's pattern of misconduct could have been halted before more Americans were harmed.

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These are not the only examples. Taken together, I am concerned that these incidents and others undermine the rule of law. The Commission must not take a similar path. We must continue to be unequivocal that violations of our orders will result in more than a slap on the wrist. Fortunately, we have a wealth of experience and a-10 (pe)du.

the FTC." US v. Danube Carpet Mills, Inc., 737 F.2d 988, 993 (11th Cir. 1984). While there is no precise formula for calculating civil penalties, these penalties should -- in the words of Chairman Simons when he led the Bureau of Competition -- "serve as a clear signal to all firms under FTC order that they must abide by those terms or face severe consequences."[13]

Additionally, I believe the FTC should hold individual executives accountable for order violations in which they participated, even if these individuals were not named in the original orders. This relief is expressly contemplated by Fed. R. Civ. P. 65(d), which provides that an injunction against a corporation binds its officers.[14] And this relief is important, because it ensures that individual executives who control the operation of the firm -- not just shareholders -- bear the costs of noncompliance.[15]

Using many of these tools, the FTC has proven itself to be an aggressive and effective enforcer of its orders. As noted in a report on the FTC's Project Scofflaw, agency efforts to prosecute serial offenders have resulted in civil and criminal contempt findings, millions of dollars in fines, and even incarceration.[16] While that project was launched more than two decades ago, the FTC's more recent efforts to pursue Kevin Trudeau[17] show that we continue to vindicate our authority and protect the public interest when our orders are violated.

In addition to vigorously using these corrective tools, we must also consider how to prevent these parties from further recidivist behavior. Here, our existing approach to resolving fraud cases offers a useful model. In these cases, we routinely impose "fencing-in" requirements to prevent future harm to consumers, including bans on adjacent business practices, bond requirements, and compliance reporting. Frequently, we also seek fencing-in relief against individual defendants, including lifetime occupational bans for recidivists.

While these aggressive remedies are typically applied in fraud cases, we should not hesitate to apply them against repeat offender corporations and their executives. Regardless of their size and clout, these offenders, too, should be stopped cold. Indeed,(e)4 (ve)4 (nt)-2 (z)-6 (D (n)-4 (a)4nnnnnn

- Dismissal of senior executives and board directors: Senior managers of firms are often quick to pin the blame on junior employees for repeated problems in the organization, but are less quick to acknowledge their own failures to remedy concerns. As noted above, orders not only bind a firm, but also its officers. When appropriate, the Commission should seek dismissals of executives and board members overseeing conduct that violates our orders.[19]

- Dismissal of third-party compliance consultants: Firms frequently hire third-party consultants and auditors to demonstrate that they are relying on independent judgment to ensure compliance with the law. However, the independence of these consultants can often be compromised.[20] The failure of a third-party compliance consultant to detect conduct that violated a Commission order may warrant their dismissal.

- Clawbacks, forfeitures, and reforms to executive compensation agreements: While equity owners should certainly incur costs when orders are violated, a fairer allocation of liability might include specific recoveries from executives. In those instances, it may be important for the violating company's board to exercise any rights it may have to claw back bonuses and order the forfeiture of certain unvested stock options and grants. In addition, the components of executive compensation arrangements may need to be amended to reflect a firm's commitment to compliance with the law.[21]

- Requirements to raise equity capital: A close investigation of a firm might determine that the underlying driver of misconduct stems from the need to generate cash to service unmanageable debt. High levels of corporate debt can amplify returns on equity, but when it creates risks to consumers and competition in the form of an order violation, it may be appropriate for the Commission to seek recapitalization of the firm, even if this means that senior executives will find that their stock holdings are diluted.

Of course, this list is far from exhaustive. When orders are violated, a key question I will evaluate when reviewing matters for consideration by the Commission is whether the proposed remedies address the underlying causes of the noncompliance. To that end, I look forward to hearing from you about your ideas for ensuring that companies stay on the right side of our orders -- and face consequences when they do not.

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[19] As noted earlier, the Office of the Comptroller of the Currency recently reiterated its rights to dismiss Wells Fargo executives and directors. See n.11.

[20] See, e.g., Agreement, NY State Dept. of Financial Services, In the Matter of Promontory Financial Group, LLC (Aug. 18, 2015), https://www.dfs.ny.gov/about/ea/ea150818.pdf; Agreement, NY State Dept. of Financial Services, In the Matter of Deloitte Financial Advisory Services LLP (Jun. 18, 2013), https://www.dfs.ny.gov/about/ea/ea130618.pdf.

[21] For example, an agreement between the Office of Inspector General of the Department of Health and Human Services and GlaxoSmithKline required the company to change its executive compensation program, including by permitting bonus recoupment in the event of significant misconduct. See Corporate Integrity Agreement between the Office of Inspector General of the Dept. of Health and Human Services and GlaxoSmithKline LLC (Jun. 28, 2012), https://www.justice.gov/sites/default/files/opa/legacy/2012/07/02/hhs-corp-integrity-agreement.pdf.