EXAMINING THE SEC'S AGENDA, OPERATIONS, AND FY 2017 BUDGET REQUEST

HEARING

BEFORE THE

COMMITTEE ON FINANCIAL SERVICES
U.S. HOUSE OF REPRESENTATIVES

ONE HUNDRED FOURTEENTH CONGRESS

FIRST SESSION

NOVEMBER 18, 2015

Printed for the use of the Committee on Financial Services

Serial No. 114–62

U.S. GOVERNMENT PUBLISHING OFFICE

99–781 PDF WASHINGTON : 2016

For sale by the Superintendent of Documents, U.S. Government Publishing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512–1800; DC area (202) 512–1800
Fax: (202) 512–2104 Mail: Stop IDCC, Washington, DC 20402–0001

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EXAMINING THE SEC'S AGENDA, OPERATIONS, AND FY 2017 BUDGET REQUEST

Wednesday, November 18, 2015

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The committee met, pursuant to notice, at 10:04 a.m., in room 2128, Rayburn House Office Building, Hon. Jeb Hensarling [chairman of the committee] presiding.

Members present: Representatives Hensarling, Royce, Garrett, Neugebauer, Pearce, Posey, Fitzpatrick, Westmoreland, Luetkemeyer, Huizenga, Duffy, Hurt, Stivers, Fincher, Stutzman, Mulvaney, Hultgren, Pittenger, Wagner, Rothfus, Messer, Schweikert, Guinta, Tipton, Williams, Poliquin, Love, Hill; Waters, Maloney, Velazquez, Sherman, Capuano, Clay, Lynch, Scott, Green, Cleaver, Ellison, Himes, Sewell, Murphy, Delaney, Sinema, Beatty, Heck, and Vargas.

Chairman HENSARLING. The Financial Services Committee will come to order.

Without objection, the Chair is authorized to declare a recess of the committee at any time.

Today's hearing is entitled, "Examining the SEC's Agenda, Operations, and FY 2017 Budget Request."

I now recognize myself for 3 minutes to give an opening statement.

This morning, we welcome back U.S. Securities and Exchange Commission Chair Mary Jo White. This committee is committed to conducting vigorous oversight of the SEC because the SEC's three-part mission is an important one as Americans continue to struggle through an economy that is underperforming.

It is on their behalf that this committee acts to ensure that the SEC protects investors; maintains fair, orderly, and efficient markets; and promotes capital formation—all key ingredients to growing a healthy economy with opportunity for all.

Vigorous oversight is also needed to ensure that the SEC is a good steward of its resources, both its time and its budget—a budget that has increased dramatically by more than 64 percent over the last 10 years, while the monitors to my left, right, and in front of me show the rapidly rising red ink of our national debt.

Since Chair White's last appearance before our committee, we have seen both good news and bad news. First, the good news. The SEC finally completed the bipartisan JOBS Act rulemakings to implement the reg A+ and crowdfunding titles. This is noteworthy and commendable.

Further, the SEC has now asserted its jurisdiction to hopefully stop the Financial Stability Oversight Council (FSOC) from regulating asset managers like banks. This, too, is commendable.

Regrettably, there is more to discuss that is not so commendable. On a three to two partisan vote, a pay ratio rule was pushed through which may appease left-wing activists, but does nothing to protect investors or facilitate capital formation for small and medium-sized businesses; and does nothing to help struggling families get ahead.

It is another example of the SEC squandering precious resources on rulemaking that, again, does nothing to protect investors or facilitate capital formation.

Additionally, as much as left-wing activists may wish to drag the SEC into political advocacy, the *Citizens United* decision does not involve or implicate Federal securities laws.

A political disclosure rulemaking is not within the SEC's core competency or, more importantly, it is not within its mission. It would simply create more opportunities for abuse and politicized enforcement, as we have seen with the IRS scandal, and further damage the SEC's credibility.

The SEC should instead redouble efforts to simplify the disclosure regime and renew its commitment to the materiality doctrine articulated by the Supreme Court in 1976.

Instead of modernizing our proxy system, the Chair's recent action to cut off staff guidance to public companies in the middle of this past proxy season was ill-advised. And the universal proxy ballot proposal favors special interests and short-termism rather than benefiting the vast majority of public company shareholders.

Finally, the SEC does have an opportunity to act and stop the Labor Department from making financial advice and retirement planning less available and more expensive for Americans with low and moderate incomes. This, we hope, they will successfully do.

Real investor protection comes from innovative capital markets that are vigorously policed for force, fraud, and deception. They allow capital formation to flourish, and give investors the freedom to make informed investment decisions free from government interference and control.

I now yield 3 minutes to the ranking member for an opening statement.

Ms. WATERS. Thank you very much, Mr. Chairman.

Welcome back to the committee, Chair White. Today, we gather to discuss the SEC's work to oversee our capital markets. This work, however, is hampered by harmful Republican cuts to your budget request, which will make it harder for you to police these markets. Please know that Democrats are committed to full funding for the SEC because the Commission provides the first line of protection for investors.

It has been 8 months since you were last here and more than 5 years since Dodd-Frank was enacted. But the SEC still has yet to propose a uniform fiduciary standard. I am pleased to learn that certainly while the Department of Labor is doing its part to create a rule that works, that you are working toward this end, and that there should be something in the reasonable future dealing with this issue.

Regarding the inadequate level of advisor exams, I join industry associations, advocates and members of this committee in calling for a modest fee on advisors and I am concerned about any costly third-party exams which your staff may be working on.

I am also concerned—well, as we have discussed, I am deeply concerned about the continued seemingly reflected granting of waivers of bad actor disqualifications. These waivers allow some of the worst actors in our financial system to continue business as usual. And I look forward to your explanation of exactly how these decisions are made. In recent times, I have learned that they are made quite differently than I thought.

Lastly, I received your letter concerning a bill we considered last week related to business development companies. While this isn't quite the bill I would have offered, we did craft a compromise that I believe addressed most of your earlier concerns with the legislation.

I also offered an amendment with Ms. Velazquez to address your new concerns with BDCs owning investment advisors. We disagree relative to the modest increase in leverage, but I urge you to help us craft language to further improve this bill before it moves to the House Floor.

Thank you, and I yield back the balance of my time.

Chairman HENSARLING. The gentlelady yields back.

The Chair now recognizes the gentleman from New Jersey, Mr. Garrett, chairman of our Capital Markets Subcommittee, for 2 minutes.

Mr. GARRETT. I thank the chairman. And I thank Chair White. It is good to see you again.

I may be echoing some of the comments that Chairman Hensarling has raised. And I do that because, frankly, the last time that you were here before the committee, I noted my concerns back then over the large number of 3–2 votes that the Commission has taken over the last several years, as well as the general perception that the SEC is becoming basically increasingly politicized.

Since that time, really little has happened to relieve any of those concerns of myself or the Chair or that others have raised. In fact, in the last 6 months, the SEC has prioritized and completed the very partisan and politicized pay ratio rule and is right now in the process, as you know, of developing a universal proxy ballot rule. In essence, these are two priorities that may appease the special interests, but they really do very little to make our capital markets more competitive.

So, while I am pleased that the SEC has at last finalized the crowdfunding provisions of the JOBS Act, I would note that this was also done along a partisan vote, 3 years after the congressional deadline.

At the same time, the SEC's ongoing failure to develop what I might call a capital formation agenda remains one of the most serious deficiencies. It seems that the only time that the SEC actually modernizes its securities laws, to the benefit of the growing numbers of businesses, is when we here in Congress tell you to.

Now, tomorrow, the SEC will host for the 34th year in a row, the Annual Government Business Forum on Small Business Capital Formation. That is good.

As in previous years, I expect this forum to produce a number of valuable ideas that will help small enterprises get capital and grow.

But as in previous years, I also expect that the majority of these recommendations will be basically ignored by the SEC.

Finally, the SEC clearly has an important mission and role within our sector, the financial sector, but right now, it is up to the agency to get its priorities in order.

And so, I look forward from hearing from you today on how the SEC can refocus on this threefold mission for the benefit of Americans's capital market.

And I yield back.

Chairman HENSARLING. The gentlemen yields back.

The Chair now recognizes the gentlelady from New York, Mrs. Maloney, ranking member of our Capital Markets Subcommittee, for 2 minutes.

Mrs. MALONEY. I thank the chairman for holding this important hearing, and I welcome Chair White.

Quite a bit has happened since Chair White last appeared before this committee in March. For starters, the SEC has finalized several rules, such as the CEO pay ratio rule, and two JOBS Act rules.

Perhaps most importantly, the extreme volatility in the markets on August 24th was the first real-world test for many of the market safeguards that the SEC put in place after the flash crash of 2010.

In particular, the automatic trading pauses for stocks that experience extreme volatility, known as the limit-up, limit-down rules, were triggered nearly 1,300 times on August 24th. And a lot of the stocks that were halted that day were exchange-traded stocks, rather than stocks of individual companies.

Many stocks that were temporarily halted had trouble opening up again, because when they opened back up for trading, their prices rose too quickly—which triggered another automatic pause.

However, despite this widespread disruption, the market-wide circuit breaks, which would have halted trading on the entire market for 15 minutes, were not triggered on August 24th.

So, I will be very interested in hearing Chair White's perspective on how these new safeguards performed. Did they work as intended? Or are there problems with the safeguards that need to be fixed?

Thank you. I yield back, and I look forward to your testimony.

Chairman HENSARLING. The gentlelady yields back.

Today, we welcome the testimony of the Honorable Mary Jo White, Chair of the U.S. Securities and Exchange Commission.

Chair White has previously testified before this committee, as we all know, so I believe she needs no further introduction.

Without objection, Chair White, your written statement will be made a part of the record, and you are now recognized for 5 minutes to give an oral presentation of your testimony.

Thank you.

STATEMENT OF THE HONORABLE MARY JO WHITE, CHAIR, U.S. SECURITIES AND EXCHANGE COMMISSION

Ms. WHITE. Thank you.

Chairman Hensarling, Ranking Member Waters, and members of the committee, first, thank you for inviting me to testify about the recent activities and current initiatives of the U.S. Securities and Exchange Commission.

Since I last testified before this committee in March, the SEC has advanced significant rulemakings, continued to bring strong enforcement actions against wrongdoers, and made significant progress on our initiatives involving the asset management industry, equity market structure, and disclosure effectiveness.

The Commission has adapted or proposed 17 substantive rulemakings in the past 8 months, including rules required by the Dodd-Frank and JOBS Acts, and these efforts have included final or proposed rules addressing: over-the-counter derivatives; new means for small businesses to access capital, including the final rules—as the chairman mentioned—both for updating and expanding Regulation A, and for allowing securities-based crowdfunding offerings; enhanced oversight of high frequency traders, and our supervision of investment advisors and mutual funds; amendments to the SEC rules governing its administrative proceedings; executive compensation disclosures; and removing references to credit ratings from our rules.

The Commission also approved a proposal by the National Securities Exchanges and FINRA for a 2-year pilot program that would widen tick sizes for stocks of some smaller companies.

Our enforcement program also continued to deliver very strong results, with the Commission bringing 807 enforcement actions, and obtaining monetary remedies of approximately $4.2 billion in Fiscal Year 2015.

Of the 807 enforcement actions filed, a record 507 were independent actions for violations of the Federal securities laws.

More important, though, than the numbers, these actions addressed meaningful issues for investors and the markets, spanned the securities industry, and included a number of first-ever kinds of actions.

Significantly, approximately two-thirds of our substantive actions in Fiscal Year 2015 included charges against individuals. The Commission also continued to seek admissions, including the first-ever admissions settlement with an auditing firm, and to pursue complex cases with criminal authorities, including a recent action charging dozens of defendants with a global scheme to profit from hacked, non-public information about corporate earnings announcements.

Going forward, we plan to continue to focus on completing our mandatory rulemakings, while pursuing other initiatives that are critical to our mission, including those relating to asset manager oversight, equity market structure, and disclosure effectiveness.

This afternoon, for example, the Commission is expected to consider new rules to enhance the transparency of equity alternative trading systems. We will also continue to strengthen our enforcement and examination programs, striving for high impact efforts that protect investors and preserve market integrity. And we will continue developing a number of ongoing initiatives designed to facilitate capital formation, particularly for small businesses.

The agency's Fiscal Year 2017 budget request to the Office of Management and Budget reflects these priorities, focusing on the execution of our core programs and operations by seeking to hire individuals with the skill sets necessary to enhance the agency's oversight of increasing complex securities markets, striving to build the significant new oversight programs assigned to the SEC in recent years, and continuing to enhance our technology, including our ability to analyze and assess large volumes of data.

As we continue to place a high priority on allocating our resources efficiently and effectively, I was very pleased that the Commission recently received an unmodified audit report, the agency's best ever audit opinion from the GAO, with no material weaknesses or significant deficiencies identified in Fiscal Year 2015.

We plan to build on these improvements and continue to enhance the execution of our mission.

The Commission's extensive work to protect investors, preserve market integrity, and promote capital formation is not limited to the initiatives I have just summarized today or in my written testimony. But I have tried, by example, both here and again in the written testimony, to convey the breadth and importance of the Commission's ongoing efforts, and provide a sense of our progress in the last few months.

Thank you for your support for the agency's mission, and for inviting me to be here today. Your continued support will allow us to better protect investors and facilitate capital formation, and more effectively oversee the markets and entities we regulate.

I will be happy to answer any of your questions.

[The prepared statement of Chair White can be found on page 64 of the appendix.]

Chairman HENSARLING. Thank you, Chair White.

The Chair now yields himself 5 minutes for questions.

Chair White, it was reported that you announced at a conference recently that the SEC is "full out focused on developing its own fiduciary rule." I alluded to it in my opening statement.

You were last here in March, and we have spoken about these matters both publicly and privately, but is it my understanding that the SEC staff has not yet performed an updated analysis of the potential impact of a uniform fiduciary standard on retail investors.

Is that correct?

Ms. WHITE. The answer is there is not another 2011 study that has been done. As we proceed with this, the staff's recommendations, which are very much in process, actively in progress—

Chairman HENSARLING. Is there any work being done to update the 2011 study?

Ms. WHITE. Part of the rulemaking, as it advances, will be very deep economic analysis by our economists at the SEC, to judge impacts, as well as all relevant baselines, and its—

Chairman HENSARLING. Will that analysis be complete before the proposal of any uniform fiduciary standard?

Ms. WHITE. Certainly, there will be economic analysis that is complete before there is any proposal. There is always additional economic analysis, as there should be, before you proceed with any adoption. But certainly, that will be part of the proposal process.

Chairman HENSARLING. But not necessarily the complete analysis that the staff is—

Ms. WHITE. Not necessarily, but it really depends on how it is assessed as we go through that process, including with our economists.

Chairman HENSARLING. Will this analysis be shared with this committee and made public prior to the proposal of any uniform fiduciary standard?

Ms. WHITE. Typically, unless there is a paper produced separately, which happens from time to time from our DERA folks, it is part of the proposal and made public in that way.

Chairman HENSARLING. We would encourage you to do that.

Chair White, I don't know if you share the concerns that many share on this committee in looking at the experience of a similar proposal in the U.K, but the public sources that I have been able to access show that when they imposed a similar fiduciary rule, 310,000 clients stopped being served by their brokers because their wealth was insufficient to advise profitably, and 60,000 investors were not accepted as new clients for the same reason.

And in the year before the Commission ban went into effect, the number of advisors serving retail accounts plunged by 23 percent. Does the experience in the U.K. concern you?

Ms. WHITE. I am familiar with several U.K. analyses. Clearly, a concern of this rulemaking is what impact does it have on the ability of retail investors to get reasonably priced, reliable advice.

And as I think I have said before, part of this rulemaking process will be very much devoted to what impact it will have on precisely that.

Chairman HENSARLING. I would hope that the SEC would look very closely at the U.K. experience, and also look at—I hope you have received similar testimony that we have received, that the best interest contract exemption is, frankly, unworkable and not an exemption at all, meaning that the U.K. experience is most parallel.

Switching subjects to bond market illiquidity, again, you last appeared before us in March. At that time, you acknowledged the concern about bond market illiquidity, and again, we have spoken about these matters publicly and privately. Since you testified that at that point, you did not see a link between the Volcker Rule, capital requirements, and reduced bond liquidity, it has been 8 months.

In the intervening 8 months, on May 20th, The Wall Street Journal reported that the number one concern of financial professionals was lack of liquidity in the markets. In August of 2015, PricewaterhouseCoopers published a study that attributed "the measurable reduction in financial market liquidity to multiple factors, including bank derisking, due to new regulatory frameworks."

Last week, The Wall Street Journal reported that U.S. firms are holding negative corporate bond inventories for the first time since the Fed began reporting this separate data.

The Chair of FINRA has testified in this committee that, "There have been dramatic changes with respect to the fixed income market in recent years that has led to much higher capital requirements, the Volcker Rule, that limits the ability for proprietary trading with respect to bank holding companies, and a range of other issues that have all had significant impact from the standpoint of liquidity of the fixed income market."

So since it has been 8 months since you last appeared before us, there has been news. Have you been able to determine whether regulations like the Volcker Rule are a contributing cause to the dramatic decrease in liquidity in our fixed income markets?

Ms. WHITE. Let me say that it remains a concern of mine, as I testified 8 months ago. I think it does of all regulators. But the answer to your question—the direct answer to your question is no, as is reflected in the quarterly reports that we make actually to this committee on that subject with our fellow financial regulators.

I think the most recent one reflects both levels of liquidity in the primary and secondary markets, as set forth there, and the conclusion that one cannot determine impact from the Volcker Rule. Obviously, there are a lot of factors including capital requirements and others that go on.

I do note that at least recently, reports do indicate that dealer inventories have gone into negative territory, and that is something that obviously we will be looking very closely at before the final report for this year. I am not trying to get ahead of the report, but we will be looking very closely at that, both for its existence, its meaning, and whether impacts can be judged.

Chairman HENSARLING. My time has expired, but Chair White, the rest of the world is concluding otherwise. So I would hope the SEC would pay very careful attention.

The Chair now recognizes the ranking member for 5 minutes.

Ms. WATERS. Thank you very much, Mr. Chairman.

Chair White, you will be asked today about your efforts on a number of issues, and I am appreciative for your response on the fiduciary duty rulemaking. But just for a second, would you please explain to us how a lack of adequate funding does not allow you to move as quickly as we would like you to move on some of these issues? Are you at all hampered by inadequate funding of the SEC?

Ms. WHITE. We clearly—and I have testified about this before—have responsibilities far beyond our resources, and so we obviously try to make the smartest decisions we can in core areas—in new areas we have been assigned since Dodd-Frank and the JOBS Act. But clearly, it becomes a zero sum game, as they say, at some point, and it does slow you down. Of course it does.

Ms. WATERS. Thank you very much. With that, I would like to just have you describe to us the SEC waiver process. The last time you testified, I expressed concern with the SEC's policy of providing waivers of disqualifications to bad actors on a seemingly reflective basis and I questioned the transparency of whether or not there should be public input.

As you know, I have a proposal that I think would remedy this problem that would, among other things, require the process to be conducted and voted on by the Commission that will provide the public a notice-and-comment period and an opportunity to request a hearing, and require SEC staff to keep complete public records of all waiver requests and denials and create a public database of all disqualified bad actors.

So here I am, even with a bill, talking about more work for you in this area. Before I go any further, because I know this is a little bit more complicated than most people think, would you explain to us a little bit about that process?

Ms. WHITE. Yes. First, I want to make it clear that the SEC very aggressively pursues financial institutions and senior corporate executives and our record bears that out during and after the financial crisis. So when it comes to disqualifications and waivers, it is very important to understand that those are not enforcement remedies. Those are separate provisions in the securities laws that are governed by their very separate rules, very separate guidances that the Commission and the Commission staff apply very vigorously, case by case.

When an enforcement action of ours or someone else's may trigger a disqualification, and then if a party is seeking a waiver, and it is typically a waiver to be allowed to pursue or continue to pursue business in a totally unrelated area, than the enforcement action was about. The burden is on that party to show us that—to simplify it a little bit it would be in the public interest to grant that waiver.

The staff, in order to increase transparency and robustness, has updated under my tenure and my direction, guidance on the WKSI waivers, as well as the bad actor waivers, and I think the Commission and the staff do very deep dives and apply those standards quite robustly before making those decisions.

If a waiver is granted, it is made public on our website. If a waiver is not granted, typically, the party will withdraw the request for that, and it includes non-public information. I think if you look at only the public record, you would think we are granting routinely in all of them, and that is not the case. There are many, many that we do not grant.

And so a challenge is preserving the privacy of non-public information, but yet, being able to provide publicly the information that shows that we are not granting these waivers as they are requested each time. It is a very robust process.

Ms. WATERS. I would like you to take a look at my legislation and see if there is anything that we could do with that legislation to help you improve the process, if you believe there is room for improvement.

Lastly, on BDCs, you have written a letter to us with your concerns. I, and others, are concerned about support for small businesses and we want to make sure that we do everything to create resources. Can you help me understand what your concerns are a little bit better and what we can do to make the bill better?

Ms. WHITE. First, let me say that I think BDCs are designed to be an engine for economic growth, particularly for small businesses, and that is good for everybody and it is something that the staff and the Commission have been supportive of throughout the years, frankly, since they were set up.

And I appreciate, by the way, that some of the concerns that I expressed a couple of years ago with the prior bill were addressed. I would be happy to talk about it further, but I did recently submit a letter to you and to the chairman expressing my concerns with certain aspects of the current bill, really investor protection concerns that are significant concerns which I felt I really must express.

Obviously, it is up to Congress what they do, essentially in several areas, but primarily, the increase in leverage, as well as the reduction of rights if I can, again, oversimplify a little bit, in preferred stockholders kind of net net, you also end up under the proposed bill, allowing a BDC to invest 50 percent of their assets in a financial institution.

That is currently 30 percent. And the core objective for the BDCs is really to invest in operating companies and new operating companies that you want to give a boost to. And these are retail investors that we are talking about who own the vast majority of BDC shares, so that obviously heightens whatever investor concerns we have.

Ms. WATERS. Thank you very much, Mr. Chairman. And I hope you will work with us to improve the legislation.

Chairman HENSARLING. The Chair now recognizes the gentleman from New Jersey, Mr. Garrett, chairman of our Capital Markets Subcommittee.

Mr. GARRETT. Thank you.

Chair White, when you were here once before, I opened with the question, "Are the markets rigged?" Let me follow up now with, is SIPC rigged as far as the coverage that you get from there? And does the small investor actually know that he has no coverage under SIPC with his statement?

Let give you a quick example. Years ago, I invested $2,000 when I came out of college in the marketplace. In over 30 years now, the market has gone up, it has grown—I have gotten dividend payments out, I have gotten capital gains, I withdrew some money over the years to pay taxes and do—likewise. So over the last 30 years, my statement says it is going up and up in value. I have taken out that $2,000 that I initially invested.

As I understand it, my SIPC coverage right now for my statement—which says I have well over that $2,000; I have about $5,000 or $6,000 in my account—is exactly zero. Is that correct?

Ms. WHITE. As I heard your scenario, that is correct because what SIPC is designed—

Mr. GARRETT. I have zero coverage, even though my statement is telling me I have like $5,000 in there, but there is a statement indication on the bottom of it that I have—SIPC coverage on a statement when I go to the broker dealer that his has a logo right there. Does anyone have an obligation to inform me that I have exactly zero coverage on my brokerage statement? Whose obligation is it to tell me that? Is that—

Ms. WHITE. First all of, your account statement should be accurate and obviously, what has sort of given rise to these concerns is a huge Ponzi scheme, where the account statements are—

Mr. GARRETT. But who should tell me that I have zero coverage right now?

Ms. WHITE. The broker should tell you, but the broker in question may be committing a massive Ponzi scheme, so you may not get that—

Mr. GARRETT. So it is a fiduciary duty of the broker to the investment advisor to tell me that I have zero coverage?

Ms. WHITE. I am not sure I could give you a legal opinion on that, but what I can say is that what SIPC covers is what securities and cash that the broker has custody of. So if, for example, in your example, when you put in your $2,000, you had invested in certain securities that had appreciated, so there were securities in the hands of that broker, they would be covered by SIPC.

But if instead, what your broker did was essentially never engage in bona fide trades, it doesn't protect against fraud, which is really what we are talking about, I think.

Mr. GARRETT. We don't know exactly what is, but I am a simple investor. I think I have this much money. I find out that something went wrong, it is not the market issue, but in actuality, your answer to the first question is I have zero coverage. There is an obligation of someone, I guess the broker, to tell me this and at that point, the wise thing for me to do would be what? To move down the street to another brokerage account, because then my coverage would go back up. Is that not correct? The full amount that I have invested?

Ms. WHITE. If you put that amount in that broker's custody, it would be covered by SIPC.

Mr. GARRETT. Right. So investors should be told that the smart thing to do once you have withdrawn the initial investment, is to move to another company.

Ms. WHITE. But keep in mind, if you have withdrawn your $2,000, but it had appreciated with securities to $7,000 and the broker had those securities and then went under, you would be protected to that $7,000.

Mr. GARRETT. Not from SIPC, however. Not from—

Ms. WHITE. You would be protected by SIPC, if in fact you had invested that $2,000 at some point in securities and it was still with the broker. But what you are not covered for is essentially these Ponzi schemes that are reflected falsely on your account statements.

Mr. GARRETT. It depends on how the investments are made, in other words? So I as an investor now need to know when I get the statement, whether the investments are being done like in a Madoff situation, or whether the investments are being done some other way. So it really depends.

How is the investor supposed to know that, whether he is really getting coverage or not then?

Ms. WHITE. Of course, the problem is in the Madoff, and it is a huge problem, obviously, in the Madoff situation is that investments weren't being made. And so you had a massive Ponzi scheme. So you were being defrauded kind of from beginning to end.

Mr. GARRETT. So the bottom line for me, as a simple investor—and that really describes me well in these things; I don't know how it is being done, and I really don't know whether SIPC is going to be there at the end of the day.

I would like to move on to a bunch of other questions on regulation D and Rule 506 under the Dodd-Frank Act, really quickly here. So you have proposed some amendments to that? And the question is, what is the effect of those amendments on the marketplace? The SEC's Division of Economic Risk Analysis said that only 2 percent, or $33 billion, of the capital raised under reg D has come under 506 of the JOBS Act, which we did.

That would sort of tell me that there is a suppression effect of your amendments just hanging out there. Can you withdraw those amendments so that we can actually get the full effect of the JOBS Act and 506(c) of Dodd-Frank?

Ms. WHITE. As you mention, there hasn't been consensus on those amendments, so they have not moved forward. I do think they are important however. I still believe they are important to give us greater information, greater clarity into how the markets are operating. Obviously, we have a year-and-a-half of operation now. We have had an interdivisional group looking at those markets.

I have also inquired about, because I have obviously heard the concern that just the fact that regulation is proposed may be hampering those markets.

Mr. GARRETT. Exactly.

Ms. WHITE. The feedback that I have gotten, at least from our folks, is that they don't believe that is the case. That is not a definitive finding. But clearly, the 506(c) market has been used, but not as much as one might have anticipated and certainly not as much as the 506(b) market is being used.

Mr. GARRETT. Thank you.

I yield back.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentlelady from New York, Ms. Velazquez.

Ms. VELAZQUEZ. Thank you, Mr. Chairman.

Chair White, recently it was reported that UBS was underwriting bonds for Puerto Rico's retirement system, and then placing the same bonds into mutual funds that were sold to customers on the island—something that would be prevented by the Investment Company Act of 1940.

However, due to the high cost of air travel at the time the Act was passed, Puerto Rico and other U.S. territories at the time, including Hawaii, were exempted from the 1940 Act. I have recently introduced legislation, H.R. 3610, to close this loophole and ensure that Puerto Rico and other U.S. territories have the same protections as States do.

Do you believe that this loophole should be closed?

Ms. WHITE. Let me say, I share your concern. I think when the exemption was put into law, it was many, many years ago when the thought was that just the practical and financial difficulties of being able to sort of enforce that law in the territories was just not there.

Today is a very different world. So I share your concerns. I think the loophole should be closed.

Ms. VELAZQUEZ. Thank you.

In the ongoing financial crisis in Puerto Rico, hedge funds are playing a significant role. It is impossible, however, to fully understand the scope of their investments. Some disclosure requirements are only available to regulators, while others do not cover debt securities or derivatives.

I recently introduced legislation, H.R. 3921, to close this loophole and increase disclosure requirements on hedge funds.

Do you believe that further disclosure in this area will benefit investors and the public?

Ms. WHITE. I think I would have to study it further, the precise parameters of it. I can see pros and cons, frankly, to that approach. Clearly, registration and reporting are critical to increasing transparency and protecting investors in private funds. And this has been looked at very closely in connection with Dodd-Frank when we were given authority over private fund advisors.

And there is a lot of information that is actually produced on Form PF by hedge funds and others.

But the judgment was made then not to basically expose or—expose more than was prescripted to be exposed, the actual holdings and strategies of private funds, whether hedge funds or not, because that could lead to front-running and other kinds of actions with respect to that kind of disclosure.

So, there are pros and cons to that. I need to study it further.

Ms. VELAZQUEZ. Okay. Thank you.

And I hope that we can work with your office at least to hear some feedback regarding the legislation.

Another issue that has come to our attention, and that I care about as ranking member on the House Small Business Committee, is that the small business online lending industry that has grown rapidly in the past 5 years, and experts are expecting double-digit growth through 2020.

Last week, I sent a letter requesting information on your agency's involvement with small business online lending. Is there anything—any preliminary comments on my request?

Ms. WHITE. I have seen the letter. We will obviously be responding to it in due course. In terms of what our space is with respect to online lending, we don't regulate the loans themselves, the lenders, and the terms of the loans to borrowers. That is not in our space.

However, we do regulate online lenders when they sell securities to investors that essentially fund these loans whether through notes or investment contracts. They may need to register the offerings. Some platforms, depending on how they do it, could have to register as broker-dealers. We have brought cases in the enforcement space on some of this. But our jurisdiction really relates to protecting investors if, in fact, their offering is made under the Federal securities laws.

Ms. VELAZQUEZ. Thank you.

I yield back.

Chairman HENSARLING. The gentlelady yields back.

The Chair now recognizes the gentleman from Texas, Mr. Neugebauer, chairman of our Financial Institutions Subcommittee.

Mr. NEUGEBAUER. Thank you, Mr. Chairman.

And thank you, Chair White, for being here today.

I want to go back to the line of questioning that the chairman was talking about, something I have had a great deal of interest in, and that is the fixed-income market. Can you tell me exactly what resources at the SEC are dedicated to the fixed-income market?

Ms. WHITE. I think we may have had this discussion at our last hearing. Primarily, it clearly is not confined to our Trading and Markets Division. And it is not segregated out as a separate unit, which I think we did talk about before. And I have had conversations—but we have 15 to 20 Trading and Markets folks who primarily deal with the fixed-income markets. We clearly have the Office of Municipal Securities, which is a relatively small office within the municipal space, which deals exclusively with that area as well.

And I have had several conversations with Steve Luparello, particularly, who is our Director of Trading and Markets, about the need for additional resources, perhaps a restructuring so that we make sure that the fixed-income markets are getting the attention that they deserve. And in his view now, and he has persuaded me, I think we are structured as we should be and resourced as we should be.

Although I will note that in our budget request, I think it is for Fiscal Year 2016—we are obviously operating under the C.R. now—we sought an additional 15 positions in Trading and Markets and at least 2 of those will relate exclusively to a study assessment of the fixed-income markets.

Mr. NEUGEBAUER. And that is in the future. But today, there are how many people doing that?

Ms. WHITE. I would say in Trading and Markets, the last time I asked for that sort of number, it was about 16.

Mr. NEUGEBAUER. But just for corporate bonds.

Ms. WHITE. Yes, it is—not counting the municipal securities, about 16 was the last number I was given. It is a rough number, Congressman, if I may say, because it is not how it is structured, because there are other people who work in the space as well who don't devote the predominance of their time to fixed income issues.

Mr. NEUGEBAUER. Back in August, PricewaterhouseCoopers released a study on what they called the "riddledness" of the liquidity in certain asset classes. And the study's findings are of concern to me as it highlighted specific areas where liquidity had measurably declined, including difficulties in executing trades, reduction in market depth, increasing market volatility, and the bifurcation in liquidity. The study also notes that pending or future rules and regulations could have further significant impact on the market-making activities as we exit or a historic period of accommodative monetary policy.

Are you aware of the Pricewaterhouse study? Have you read that and looked at it?

Ms. WHITE. The answer is, I have read a number of studies, and I believe that one as well, and certainly our staff has. And it is also something that really both in the Trading and Markets area and the Investment Management area that we have been very attuned to and in dialogue with market participants about those risks and those eventualities, particularly when interest rates go up.

Mr. NEUGEBAUER. So market liquidity is a pretty big deal, isn't it?

Ms. WHITE. It certainly is.

Mr. NEUGEBAUER. I think the concern that I have and I think others have is we are not sure that your agency is giving the attention to it. Because we hear from a lot of different market participants that the liquidity issue is a real deal.

And so I would hope as you move forward, that if you are doing studies in that area, you would share some of the findings with this committee.

I want to move to—in 2015, Commissioners Stein and Piwowar released a statement supporting proposals to shorten the trade settlement cycle for certain security transactions. Industry groups and the Commission's Investor Advisory Committee encouraged the Commission and market participants to move forward on reducing this settlement cycle, citing that it would improve investor protections and reduce systemic risk. Additionally, an industry-led committee of members across the securities industry issued a White Paper outlining the timeline in actions required to move from T-3 to T-2 settlement cycle for transactions in the United States in the third quarter of 2016.

Do you agree with moving to T-2?

Ms. WHITE. Yes, is the direct answer. We actually responded to a letter, I think it was from SIFMA and maybe others as well, to me. I think the letter was addressed to me, as to both the position that I took on it, and also asking for regulatory support to help bring that about.

And so my letter was quite supportive. It is public. We can certainly provide that. And I think the only thing I wanted to be sure of is that it didn't foreclose possibly, down the road, an even shorter settlement period.

Mr. NEUGEBAUER. Why haven't you all acted on that?

Ms. WHITE. I think it is not timely to act on it. But we will act timely.

Mr. NEUGEBAUER. What is timely?

Ms. WHITE. Essentially we are—again, the letter reflects this. We are—because I think they have gotten traction. We are allowing the industry coalition, if I can call it that, to get to the place where their systems can actually accommodate the T+2, and so the regulation they need will be in place by the time that happens, so, 2016.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentlelady from New York, Mrs. Maloney, ranking member of our Capital Markets Subcommittee.

Mrs. MALONEY. I thank the chairman.

Chair White, as I mentioned in my opening statement, I am interested in the events of August 24th, in the markets. The extreme volatility of that day meant that the SEC's automatic trading halts for individual stocks were triggered nearly 1,300 times, and I know the SEC has said that it is collecting data as quickly as possible to analyze what happened, and to determine if there are any changes to the agency's rules that are necessary.

Can you give us a sense of where this preliminary review—what you have found in this review?

Ms. WHITE. Yes, it is well along, and I am expecting that we can share some initial results from that review in the near-term. I think—and you are absolutely right as you commented earlier, we didn't invite the mini stress test on August 24th, but we had one. The markets did perform quite well, but clearly there were issues that came out of that, and one of the significant ones was obviously the market-wide circuit breakers, as you said, were not triggered, given the amount of volatility, the timing and so forth.

But we did have a large number of limit up, limit downs trading pauses, and particularly, with ETFs. Most of them were in ETFs, although interestingly, not on all ETFs. And so, even with the same underlying security, it is a more complex issue, which we are studying. In part what we are looking at is the practical operation of our rules. Obviously, we have the limit up, limit down rules in place, which were put in place as a volatility moderator after the flash crash.

It is on a pilot basis, and so, one of things that we are very, very interested in is the data that comes out of August 24th, as to what modifications, if any, what calibrations should be made in the limit up, limit down rules. We are looking very closely at the opening of the markets as well, because that is when the majority of all this occurred, and there were somewhat delayed openings, particularly on the New York Stock Exchange.

Mrs. MALONEY. Will this information or this analysis be available before the end of the year?

Ms. WHITE. I hope it will be. I don't want to commit to it, but I would hope it would be.

Mrs. MALONEY. Last December, you outlined a comprehensive plan to update the regulatory regime for asset managers in order to account for the significant changes that this industry has undergone in recent years. The SEC has now proposed two of the rules that you promised: enhanced disclosures; and the liquidity management rules that you proposed in September.

But we still haven't seen the third rule yet, which will require transition plans for winding down asset managers.

Can you give us an update on this third rule, and when can we expect this rule to be proposed?

Ms. WHITE. I think the next in the series—and this obviously—it could change, but just in terms of the workflow, will probably be the rule on derivatives.

And then, following that, would be the transition roles and also stress testing, which are—it is really—I think categorize it as three, but it is really sort of five separate areas.

And so, in terms of the transition planning rules, which are essentially designed to have funds in the industry be able to deal with disruptions in their business in an optimal way.

That will not be this year, I think in terms of a proposal, but I would hope it would be relatively early into next year.

Mrs. MALONEY. Okay. In terms of the stress test, would you expect the SEC to propose a stress test rule for large asset managers? And what are the challenges that you have encountered in developing stress tests for large asset managers? Why is it such a challenge?

Ms. WHITE. It is a challenge and it is also—it is probably the fifth in the five that I mentioned. And the staff is working on them all at the same time and working very hard on it.

Asset managers are not banks, and so one first can't just transfer stress testing for banks into this space, and so to come up with a meaningful test for very different funds with different kinds of assets, different kinds of stresses that matter is a real challenge.

But we are working very hard on it. It is actually a requirement under Dodd-Frank.

Mrs. MALONEY. Okay. Lastly, I would like to ask you about the SEC's use of administrative proceedings. And as you know, Dodd-Frank expanded the SEC's authority to try cases in an administrative forum where decisions are made by law judges rather than always having to go to Federal court, which is expensive and time-consuming.

Some critics have claimed that the SEC's administrative proceedings amount to an unfair "home court advantage"—and some have even claimed that they deprive defendants of due process. Can you speak to these issues? How do you feel about it? Do you think the SEC does get an unfair home court advantage when they are in the form of administrative law judges? And what protections are in place to ensure that defendants are still receiving their full due process?

Ms. WHITE. Administrative proceedings and administrative law judges have been used by the SEC for many, many years, as well as other Federal agencies. Congress obviously gave the SEC as well as other Federal agencies the ability to bring enforcement cases in either district court or administrative proceedings.

With respect to the SEC, we have a lot of expertise in our administrative law judges. They deal with very technical kinds of issues.

They are impartial and they have unique due process rights, not the same as a district court, but for example, unlike in district court, if you are a respondent in an administrative proceeding, you would provide Jencks and Brady material, which is essentially exculpatory information. That is not required in district court, we turn over all of our unprivileged investigative file.

We have also proposed actually for notice and comment amendments to our rules of practice to provide additional rights for defendants.

Chairman HENSARLING. The time of the gentlelady has expired. The Chair now recognizes the gentleman from Missouri, Mr. Luetkemeyer, chairman of our Housing and Insurance Subcommittee.

Mr. LUETKEMEYER. Thank you, Mr. Chairman. Chair White, thank you for being here today. And I want to start off my questions with regards to designation of insurers, insurance companies as SIFIs. As chairman of the Insurance Subcommittee, it is concerning to me as we continue to discuss this issue with a lot of the insurance industry folks as well as those insurance companies that have been designated.

Can you tell me the specific standards that you looked at whenever you voted in favor of designating two of our domestic companies as SIFIs over the objection of the insurance expert on FSOC?

Ms. WHITE. I think we may have talked about this in March as well. I participated, I think, in the AIG and the MetLife cases, not the others. Let me just—

Mr. LUETKEMEYER. I am aware of that. That is why I said just—

Ms. WHITE. That is why you said two. And the MetLife designation, as you know, is in litigation, so I am somewhat limited as what I can say. But what I can say, because the statutory criteria are in the statute in public, FSOC's guidance as to what it looks at is public. And then—

Mr. LUETKEMEYER. Okay. My question, though, is what standards did you look at that were different or more significant to you than what the insurance expert on FSOC said were not something that in his eyes rose to the level of designated as a SIFI?

Ms. WHITE. Well—

Mr. LUETKEMEYER. Where is the—to you the alarm or the—

Ms. WHITE. It is so hard to get into the—into granularity on that, I think, but obviously, we get very detailed presentations and analyses from the staff. We have a standard we are applying, and looking for certain criteria, I was satisfied that those were met in that instance.

Mr. LUETKEMEYER. Okay. One of the questions—

Ms. WHITE. Listen—I must say listening very carefully and respectfully and understanding the knowledge that the insurance representative brings to bear on this.

Mr. LUETKEMEYER. But you still went without—or went against—

Ms. WHITE. I made my independent decision, yes.

Mr. LUETKEMEYER. Okay. The other question that we always get is—our concern that we always get from insurance industry folks is we need an off-ramp, we need some way, some sort of mechanism or a delineation of things for them to do to become de-designated. Will you support something like that?

Ms. WHITE. It exists to a degree. It is important to know that because there is actually an annual review process of any company that is designated. I think what—

Mr. LUETKEMEYER. With all due respect, Madam Chair, that is not a delineation of things for them to do; that is just a report of where they are at. It doesn't tell you what—

Ms. WHITE. Well, yes. What a company that is designated will have received is a very detailed analysis of the basis of the decision of designation.

Now in some cases, in many cases, you may have a situation where it is essentially the core business model, and how much leverage is used or the kind of derivatives that are used.

And so there hasn't been a delineation. It could be difficult in many cases to do it, but the bottom line for me is, I think the clearer that we are in FSOC about what it is that could get you designated—

Mr. LUETKEMEYER. The concern that we have—

Ms. WHITE. —and de-designated is a good thing.

Mr. LUETKEMEYER. The concern that we have, though, is that there is a rubber stamp effect with FSOC with regards to insurance SIFIs. When you have the insurance expert on FSOC say no, it is not a problem, and yet everybody else goes along with the international designation versus what we think is good for our companies here in this country, it raises some questions and concerns.

Ms. WHITE. All I would say is I don't think—there is a not a rubber stamp; it is an independent decision in my view, clearly.

Mr. LUETKEMEYER. I appreciate the comment. I would venture to disagree with that at this point. Also, SIFI designation for asset managers seems to be headed down that same road, our asset managers being designated as SIFIs headed down that same road. We are very concerned about that as well. FSOC has decided to look at activities and products of asset managers. Does that concern you at all?

Ms. WHITE. Again, FSOC hasn't ruled out designations of asset managers, but I think the pivot, if I can call it that, to products and activities that may raise potential systemic risk makes sense.

Mr. LUETKEMEYER. Do you believe asset managers are systemically important?

Ms. WHITE. As phrased that way, I don't think the business model in general creates that. And it is not confined to asset managers. Securities lending is one of the activities being looked—

Mr. LUETKEMEYER. Okay. I guess my question is, do you believe the business model of asset managers can be systemically important?

Ms. WHITE. As a business model it is an agency model and therefore I think that it ordinarily would not be.

Mr. LUETKEMEYER. Interesting. I see my time is about up. I yield back. Thank you, Mr. Chairman.

Chairman HENSARLING. The gentleman yields back. The Chair now recognizes the gentleman from Massachusetts, Mr. Capuano, for 5 minutes.

Mr. CAPUANO. Thank you, Mr. Chairman. And thank you, Madam Chair, for being here.

Madam Chair, in the last, oh, I don't know, 20 years, do you know which issue at the SEC has received the most comments of any?

Ms. WHITE. You are probably going to tell me political contributions.

[laughter]

Mr. CAPUANO. I am not going to tell you anything—

Ms. WHITE. I don't know. I don't know the answer to that.

Mr. CAPUANO. My understanding is political contributions has received over a million comments—

Ms. WHITE. It has received over a million, and I think 2,000 of those are unique. So that is a lot of comments.

Mr. CAPUANO. Right.

Ms. WHITE. No question.

Mr. CAPUANO. And that being the case, again, I am asking do you plan on addressing that issue in the foreseeable future?

Ms. WHITE. Essentially, and I know we had this conversation last time as well, there are very strong views of both sides of this issue.

I think I have three, actually three fairly recent outstanding letters from members of this committee, two different letters, and some Members of the Senate as well; I will be responding to those.

But as I have said before, our focus is on, and our regulatory agenda focuses on congressional mandates and what I consider to be mission-critical initiatives. Asset management, I have mentioned the disclosure effectiveness initiative, and equity market structure—

Mr. CAPUANO. Will the disclosure—

Ms. WHITE. But I want to make clear there are avenues through the SEC's rules, which is the shareholder proposal route to raise these issues. And they are raised quite actively and the staff—

Mr. CAPUANO. They are raised, but—

Ms. WHITE. —essentially doesn't permit exclusion of them.

Mr. CAPUANO. They are raised, but they are not required by the SEC.

Ms. WHITE. There is not a mandatory disclosure rule. No, sir.

Mr. CAPUANO. So therefore, voluntary, which is great—there are some people who are good citizens who like to tell people what they are doing, but there are a lot who are not.

Ms. WHITE. And companies are voluntarily making those disclosures.

Mr. CAPUANO. And I applaud those who have done it voluntarily. No regulation is done because everybody does it voluntarily. All regulations on every group are done because there is always a handful of people who are not good players.

Regulations are not targeted to everybody because everybody is a bad player; all regulations, including SEC regulations, are targeted because there is always a handful of bad ones. The fact you have some voluntary compliers, that is good and I applaud them. Nonetheless, you have many that are not.

And you say, obviously—and I appreciate the fact that you clarified that you are trying to focus on congressionally-mandated one, but your disclosure effectiveness review generated I believe 64 comment letters—64 versus 1.2 million. And by the way, as I understand it, of those 64, 10 of them related to corporate political disclosures. So Madam Chair, I would suggest—

Ms. WHITE. We will undoubtedly get more comment letters as the disclosure effectiveness proceeds, but at least a couple of those letters that, you are right, were submitted on political contributions in connection with that initiative, also urge us to focus first on our congressional mandate.

Mr. CAPUANO. Clearly, I think America has spoken in every capacity they can to you and to your organization that they want to prioritize this. It is not that difficult. And the fact that you refuse to do it just kind of raises lots of questions.

But you also say you want to focus on congressionally-mandated ones. What about Dodd-Frank Section 956(a)? You haven't focused on that.

Ms. WHITE. The incentive compensation rules.

Mr. CAPUANO. Yes.

Ms. WHITE. The incentive compensation rule is a joint rulemaking with our fellow regulators and we are very active—there had been a proposal sometime ago before I even got to the Commission.

Mr. CAPUANO. In 2011.

Ms. WHITE. Correct. And we are all working on it very, very actively as we speak.

Mr. CAPUANO. 2011, 2015, almost 2016, and you think that is active?

Ms. WHITE. I am describing the current state of affairs. We are working on it very actively. The SEC is participating in it very actively—

Mr. CAPUANO. When do you think you might have a final response?

Ms. WHITE. We are working very hard to come together on that in the very near future.

Mr. CAPUANO. In the very near—

Ms. WHITE. In the very near future.

Mr. CAPUANO. Is your definition of "very near future" the same as mine?

Ms. WHITE. I don't know. But it is the very near future nevertheless.

Mr. CAPUANO. Madam Chair, those are two issues, one of which is congressionally mandated, and by the way, it said 9 months after passage. You did have a proposal, your predecessor had a proposal in 2011, as normal, and went back.

Since 2014, the other regulators have come up with a conclusion, and it is the SEC that is holding this—

Ms. WHITE. No, actually, all of the regulators are working on this jointly, and we are covering sort of the entire swath of different registrants, different kinds of registrants. It is quite complicated, but it is all of us working on this together, it is not the SEC holding anything up.

Mr. CAPUANO. —but, first of small, it is not complicated to simply require political spending to be disclosed. That is relatively simple. If you and your staff can't do it, let me know. I will have it for you in a week. It is relatively simple.

As far as the compensation, I want to be really clear: It only applies to companies with assets over $1 billion. That is all it does. It doesn't say how much, pay anybody you want any amount you want, we simply want to make sure that the incentives don't encourage companies to endanger this economy again. That is all it is.

Ms. WHITE. Absolutely. That is all it is, although how you bring that about so it will be effective is not so easy.

Mr. CAPUANO. I understand that, but something is always better than nothing. And my time has run out. Thank you, Mr. Chairman, and thank you, Madam Chair.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentleman from Michigan, Mr. Huizenga, chairman of our Monetary Policy and Trade Subcommittee.

Mr. HUIZENGA. Right here, Chair White.

Ms. WHITE. I never can find you.

Mr. HUIZENGA. Yes, I know. It is the new construction. We are about a mile away.

So, a couple of things. Actually, the seat that you occupy today was filled yesterday by Minister Evode Imena, who is the minister of mines for Rwanda. And we had a hearing on conflict minerals, Section 1502, it was—he was accompanied by the ambassador, Mathilda Mukanatabana.

I'm very concerned about the effects of conflict minerals in 1502, what effect it is having on Central Africa. And as you may recall, it is not just the Democratic Republic of the Congo (DRC), there are nine other countries that are covered by this.

As he put it, it is not a conflict minerals boycott but rather an African boycott the way that 1502 has been implemented. And you had said so yourself; I will spare you the whole regurgitation of your own speech from October of 2013, but you said, "but as the Chair of the SEC, I must question as a policy matter using the Federal securities laws and the SEC's powers of mandatory disclosure to accomplish these goals," referencing the goals which I think we all share, and certainly you and I do share, of making sure that the laudable goals of reducing conflict, keeping extortion out of the marketplace and those kinds of things is very true.

There was a letter that I, along with Chairman Hensarling, Chairman Royce, and Chairman Garrett sent you on February 25th. Your response letter stated that in the time period of July of 2010 through the middle of March of 2015, this year, the SEC had expended over 21,000 hours and spent approximately $2.7 million on this particular provision, with which I think we agree the SEC has little or no experience.

The hearing brought really two questions to mind for me. First and foremost, is 1502 really truly achieving the objectives that I think many of us agree on, of helping the people of central Africa, giving them a better life and a better opportunity?

I will tell you that Minister Imena not does not believe that is the case, they are investing more money into compliance than what their entire budget is for going out and exploring new mining possibilities.

The Washington Post had said that—they did a story on the conflict minerals rule, saying it is well-intentioned but "set off a chain of events that has propelled millions of Congolese miners and their families deeper into poverty." So that is one issue.

The second is, is the SEC the right agency to pursue and enforce these rules in light of all of the other important investor protection actions that do fall under your mandate?

My friend—I see he has just left, but my colleague from Massachusetts who was just beating you up about 956(a) that has been awaiting action since 2011, resource extraction, CEO pay ratio disclosure rules, all of those other things that have had time and attention but are not doing anything to make sure that investors are protected.

I just—I really am struggling with how this is an important element to you when we are seeing—and I understand you are being mandated to do these things, but we are seeing faster action on those that we are on 956(a) or on so many other areas that we need to have a regulation. So please help me understand.

Ms. WHITE. First, that rule was proposed before I got here, so some of those—

Mr. HUIZENGA. I fully understand. You are implementing—

Ms. WHITE. I am not trying to—I am just saying—

Mr. HUIZENGA. —you are implementing what has been given to you.

Ms. WHITE. —the early history I don't know, but I believe it contains also a deadline where some of the others may or may not, but that is just a fact.

To some degree, kind of in both directions, I sometimes get at cross purposes because of my view of congressional mandates which is I do believe we have to carry them out and to do it in the most cost-effective ways we can.

In terms of sort of what is in the queue when you can do some prioritizing, but it is also—what I did when I first got here was, because we had a lot in the queue, was to try to get separate work streams going. And so for example, the 956 rulemaking is not done by the Corporation Finance Division as this one is, but separate work streams. And so as they are ready, we proceed with them, we do them as well as we can.

Some of the time and dollars are really because we are—we have to be true to the statutory prescription and to do it as well as we can.

Mr. HUIZENGA. I understand. And in my last remaining 5 seconds, we have seen the SEC budget increase 35 percent since 2010, 64 percent since 2005, and 300 percent since 2000. And I think, I hope you are hearing from me and my other colleagues on both sides of the aisle that we need to have priorities and we may not be having to increase budgets if we would focus in on what your core mandate is. And that is what I want to encourage you to do today.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentleman from Missouri, Mr. Clay, ranking member of our Financial Institutions Subcommittee.

Mr. CLAY. Thank you, Mr. Chairman. And thank you, Madam Chair, for attending today.

And in fairness to the SEC's budget, it does not contribute to the deficit of this country, is that correct?

Ms. WHITE. That is correct. It is deficit-neutral.

Mr. CLAY. And let's stay on budget. The House and Senate appropriations committees marks for the SEC's Fiscal Year 2016 budget represent level funding, ignoring yours and the President's request for substantial increases.

Please describe what would be the effect of the SEC—of level funding in Fiscal Year 2016. What initiatives would you not be able to pursue?

Ms. WHITE. I think any number of initiatives. I think we are talking about budget in terms of budget increases over time. We also have to look at what happened to our spaces of responsibility, both the new spaces like crowdfunding and other areas but also the complexity of the markets and how much they have grown. And so what you see in our budget—and I do try to do this very carefully—is to prioritize our core mission.

We have a lot of core missions because that is the nature of the SEC, so there are a number of things that we could not proceed with if under the current C.R., for example, we are essentially in a hiring freeze which means that just as we need to expand to cover crowdfunding, for example, you know, we can't get those skilled personnel who are so important to our initiative.

It will hurt enforcement, it will hurt exams, it will hurt our IT development and enhancements, which is so critical to us being an effective regulator.

Mr. CLAY. And how does your budget compare to the industry you are regulating? Has it kept pace with the growth in the financial services industry?

Ms. WHITE. We are outmatched. No question about it. I think one metric that sort of makes the point very dramatically is that it has been reported that 6 of our largest registrants spend about $10 billion a year on technology.

Our entire budget is $1.5 billion.

Mr. CLAY. And at this time—and you mentioned crowdfunding—do you expect to need additional resources to oversee these entities?

Ms. WHITE. Yes. We have to build up that entire regime as well as municipal advisors and others.

Mr. CLAY. Thank you, Madam Chair.

And at this time, Mr. Chairman, I would like to yield the remainder of my time to the gentleman from Massachusetts.

Mr. LYNCH. Thank you. I thank the gentleman from Missouri.

Madam Chair, thank you for being here. I know that the ranking member spoke earlier in the hearing about the well-known seasoned issuer (WKSI) waivers and I know you made some comments recently regarding that.

The idea, though—the basic idea, here, is that we would reward good behavior with the WKSI title or label, a well-known seasoned issuer and also allowing them off-the-shelf registration. And yet we would withdraw that—we would withdraw that privilege if we had felony conviction or securities fraud on the part of these companies.

And so, what we have seen here repeatedly, I must say from the SEC, is that even though they are convicted of felonies, even though they are convicted of securities fraud, we let them have that privilege. We don't discourage bad behavior. And so, I am just asking you to try to explain that because I read your statement but it is confounding to me.

Ms. WHITE. Again, I have tried to lay this out and I made a speech like last March on this—

Mr. LYNCH. I read it.

Ms. WHITE. —to be as clear as one could be. But first of all, I think we are all about trying to punish bad behavior and particularly financial institutions and senior executives who have committed wrongdoing, and I think our record in enforcement is quite aggressive and quite impressive.

In terms of WKSI, essentially, that was part of offering reform. That had a somewhat different more streamlined set of procedures—if I can call it that—for well-known seasoned issuers, not just financial institutions, manufacturing companies, et cetera.

In addition to streamlining, it also provides more information real-time to investors. That is kind of the WKSI regime. In terms of, if a company is indicted or commits securities fraud or some other trigger for being disqualified as a WKSI.

And, again, this is covered by regulation or statute with respect to all disqualifications.

Then, what we also have covered by statute or regulation, is a procedure for granting a waiver, putting the burden on the party seeking the waiver. And in terms of the WKSI, what you are looking most closely at is, can you rely on the entity's disclosures going forward? The reliability of the disclosures.

So if the trigger happens to be—

Mr. LYNCH. My time has expired. What I am saying is, a conviction for fraud—a conviction for a felony, that is reason to be less reliant—that hurts the reliability of these companies, and they should have that title withdrawn from them.

That is my argument.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Wisconsin, Mr. Duffy, chairman of our Oversight and Investigations Subcommittee.

Mr. DUFFY. Thank you, Mr. Chairman.

And welcome, Chair White. It is great to have you back.

We talked privately, and I have seen the press release from the SEC in regards to the tick size pilot program. You have implemented a 5-month delay. We have talked about that. This is not going to be a death by 1,000 delays, is it? You are still committed to implementing the pilot program?

Ms. WHITE. We are totally committed to it. We want to get it right, though, so it will be meaningful, obviously. That is the goal.

And we thought long and hard about it. We calibrated the extension so that we can get good reliable data so we get the results we are hoping for from the tick size pilot. We are totally committed to going forward with it.

Mr. DUFFY. And we want good data as well and to make sure the pilot program is set up correctly. A little more time isn't met with a big objection from us, just as long as you are still committed to implementing the pilot program.

So, thank you for that. I want to follow up on the chairman's question in regard to the corporate bond liquidity and its relationship to the Volcker Rule. We think there is a great tie in to economic growth and job creation through the corporate bond market.

And, I think, you indicated today and in your last testimony that you don't see a correlation between the Volcker Rule and the lack of liquidity in the corporate bond market.

Is that correct?

Ms. WHITE. That has been the conclusion of each of our—the joint agencies, including ours—quarterly reports to this committee.

In terms of not being able, certainly, to determine that it is, I think is a better way to say it perhaps.

Mr. DUFFY. Let me be clear first.

You would agree there is a liquidity issue in the corporate bond market?

Ms. WHITE. I agree that there is a concern, yes. I think we try to give in each quarterly report exactly what we are seeing in the liquidity and sometimes it is quite strong and sometimes it is somewhat more volatile. I keep a close eye on it, and it is a concern.

Mr. DUFFY. So if not the Volcker Rule, then what? What is causing the lack of liquidity?

You have to ask the question; it has to be a concern for you. What is causing it?

Ms. WHITE. Again, I think you have to look at whatever particular market we are talking about, and a particular point in time, and assess what is the liquidity? Because sometimes there will be—talk about the lack of liquidity and it is quite robust at that time. So that is why in those reports we do both—here is what we are seeing in the primary markets, here is what we are seeing in the secondary markets.

And then, also try to analyze what is having an impact on that? Everybody is keeping a very close eye on the diminution of liquidity, which is of great concern to everybody.

Mr. DUFFY. And it would—

Ms. WHITE. But ferreting out impacts is not easy in that space.

Mr. DUFFY. There is great liquidity, but you hit a bump in the road, and all of a sudden liquidity vanishes. I think that is the cause for concern.

And so, you can say, yes, sometimes there is great liquidity—that is true. But we care more about those little bumps that liquidity vanishes, and I think a lot of us would argue that the liquidity issue has arisen with Volcker and Basel and all the rules and regulations that have come to pass.

And, I don't know if you don't want to share your personal opinion because it might be contrary to the position of FSOC—I get that, but—

Ms. WHITE. No, no. It is not that. I really do bore into this with our own staff too, because one thing that we do for every single rulemaking we do is to try to judge those impacts—

Mr. DUFFY. I would argue that there are people on the outside, per the questions by the chairman, who have some significant disagreement.

I only have a little bit of time left. I want to make just a quick comment in regard to the corporate political spending.

Obviously, I get a lot of letters, as well. I know that people rally. Folks around the country, whether they are on the right or the left, send me letters. I am sure you get the same and you know where those letters come from.

There is a political agenda. But, for a corporate political spending disclosure—would that protect investors if you did a rule to that effect? Would that be material to decisions investors make?

Ms. WHITE. That may be, to some degree I suppose, in the eye of the beholder. But clearly if you are looking for what is material to investors under current law in the particular context of a particular company it could be a certain level of spending or something else unique about a company.

If it is material now, it has to be disclosed. What is being sought is a mandatory disclosure rule across-the-board.

Mr. DUFFY. Right. This isn't material in regard to investment decisions that are made. This is politics.

Politics are coming into play, and they are trying to send a whole bunch of letters to you so we can find out how corporations might give politically, and they can rally protests and sit-ins, and we know how the game works. But I would encourage you to push back and keep a sound, steady course.

I want to quickly pivot. We had the Director of Investment Management, David Grimm, here before the committee. I don't know if you watched that testimony, but we talked to him about the systemic risk of asset managers and how FSOC had actually used your team and his team to get insight.

And I didn't feel very confident that the expertise within the SEC has been tapped by FSOC, and it gives me concern that we have FSOC making decisions that are contrary to those experts in the field, say at the SEC with asset managers also as Mr. Luetkemeyer brought up, Mr. Woodall voted against MetLife and others.

And those who don't have that expertise are voting to designate. So, we do have—and I know my time is up.

Ms. WHITE. I would just say that staff is providing extensive expertise that the FSOC on the subject of asset managers is, in terms of, for example, the request for information that went out in December. That is quite active, and it is very important that we do provide that expertise. I think it is being received.

Mr. DUFFY. I didn't feel very confident through—

Chairman HENSARLING. Time.

Mr. DUFFY. I yield back.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentleman from Massachusetts, Mr. Lynch.

Mr. LYNCH. Thank you, Mr. Chairman. And thank you again, Madam Chair, for being here.

I would like to revisit a topic that Mrs. Maloney from New York raised earlier today, and that is going back to the August 24th problems in the market. I realize at that time our markets, U.S. markets, were responding to a sell off of Chinese stocks earlier in the day. However, according to The Wall Street Journal, there were dozens of exchange traded funds that traded at shop discounts to their net asset value, or their component value, leading to outsize losses for investors.

And I know your opinion was that the markets work very well but there are some retail investors here that are very upset. Do we have any sense of how much money retail investors lost on the 24th of August?

Ms. WHITE. Not as a net, net figure, I think. Because—and particularly if you are trying to tie it to—

Mr. LYNCH. Ballpark?

Ms. WHITE. I would have to get back to you with whatever we could do on that, but with respect to ETFs themselves, clearly, you worry about retail investors in whatever spaces they are in. And they are obviously in ETF spaces, and one of the interesting things that I think will come out in our initial results when they are made public is why some ETFs with kind of the same characteristics didn't have that phenomena occur and others did.

Mr. LYNCH. Right.

Ms. WHITE. Clearly, we are looking very closely at it.

Mr. LYNCH. Reclaiming my time.

Ms. WHITE. Sorry.

Mr. LYNCH. I know that we have a couple of indices here, I guess. The Vanguard Consumer Staples ETF and the $5.8 billion Vanguard Healthcare ETF both plunged 32 percent within the opening minutes of trading, and yet if you look at the component stocks within those baskets, they were only down about 9 percent.

So what was also troubling, at the same time the VIX, the CBOE Volatility Index—went dark, so for that first half hour—it didn't come on until 10 o'clock, and people didn't know how much fear was in the market, or what direction things were going in. So that was a problem.

And this is all in a time when the Dow experienced its largest point drop in history. And so a couple of questions I have are this.

Again, I ask you, how much was the loss for retail investors? And I appreciate if you can get back to me on that. But, given the fact that the whole idea of ETFs was to respond to the flash crash, and the lack of liquidity, so people could actually trade.

We have examples of—in the first 37 minutes, there were, I think, 1,300 stops instituted on individual stocks, and—

Ms. WHITE. I think that number covers the ETFs as well.

Mr. LYNCH. Yes. Just, how can we prevent this problem? Because we are going to have sell-offs in China again, at some point.

Ms. WHITE. Again, not commenting on the cause or causes of August 24th. But what you are referencing now, at least primarily, I think, is the limit up/limit down mechanism put in after the flash crash, and that is precisely what we are studying, based on that data that was generated on August 24th, and how to recalibrate that to make it more effective.

The circuit breakers actually weren't triggered—

Mr. LYNCH. Why the delta in the component stocks, versus the ETFs? Why?

Ms. WHITE. That is exactly what we are looking at. But it is not a simple analysis, because you will have other ETFs with the same characteristics that didn't experience those trading pauses. So why is that? And that is one of the things we are analyzing as well.

And as I say, this will be an ongoing study. But I am hoping, in the pretty near future, we will be able to share some results that will answer some of the questions.

Mr. LYNCH. Yes. Do you know if in the beginning, in your talk about the opening, that was a real problem? Do you have any correlation—at least, evidence that high-frequency traders jumped on this in the early opening?

Ms. WHITE. Again, we should wait for the initial results, because we are analyzing everything, but that doesn't pop out.

Mr. LYNCH. Thank you.

And I yield back.

Chairman HENSARLING. The gentleman yields back.

The Chair now recognizes the gentleman from Pennsylvania, Mr. Fitzpatrick.

Mr. FITZPATRICK. I thank the Chair for the recognition.

And, Madam Chair, thanks for your testimony here today.

As Members of Congress, we listen to our constituents, we learn a lot about the economy, about what is holding it back, what the problems are with job growth in the country.

And 4, 5, 6 years ago, what I used to hear about from my constituents was high health care costs, high taxes, and a lot of uncertainty in the Tax Code. I have to say that over the course of the last 2 years, the focus has shifted dramatically, and almost exclusively, to the cost of regulation.

Last week, I was back home in Bucks County, Pennsylvania. I met with a constituent whose clients are banks, and he talked about this one particular new startup—about 10, 12 years old.

I think there are less than 50 employees in the bank. He said eight of them were compliance individuals, complying with regulation. I have to say, even as much as we pay attention, I was shocked at the numbers.

And those banks would tell us, these are individuals who are not able to be processing loans or meeting with customers. Last night, I met with a constituent not in the financial services industry, in a different industry, but with the same issue. He was emphatic about the cost of regulation and what it was doing to his particular industry.

In my community, Bucks County, Pennsylvania, we have a lot of high-tech biotechnology firms, startups, investors taking big risks for them.

About 3 years ago, one of my constituents from a pharmaceutical company—which employs many of my constituents—named Jeff Hatfield testified before our Subcommittee on Capital Markets, and I have his testimony here.

And what he was testifying on was the cost of regulatory compliance, the negative impact on research, hiring, and potential growth. Specifically, one remedy that he cited was the filing status classification 12b-2, to encourage growth, but also protect investors.

As I am sure you are aware, biotech companies may research new therapies for years at a great cost without seeing an actual profit, despite a lot of market valuation.

They are still required to comply with all of the regulatory requirements. He was talking about 12b-2, I think he also testified about 404(b), which is a section of Sarbanes-Oxley that requires an awful lot of sort of external audits of internal controls.

The SEC, I am sure, is looking at this. What are your thoughts on what Jeff Hatfield testified before the committee, and whether or not this cost is really dragging down innovation and hiring in the communities?

Ms. WHITE. What we do at the SEC is really quite vigorous cost-benefit analysis, and that is of all of our rules. I think one of the great success stories of the SEC, frankly, is our Division of Economic and Risk Analysis (DERA) unit, our economists who actually perform that work and a lot of other work at the SEC, a lot of studies to try to really calibrate both the baseline—where are we now, in terms of what are we trying to accomplish with the regulation, what is the benefit of that, where is the market now, and then, if we impose this regulation in this form, what is its cost going to be?

And you clearly look at the size of a company when you do that, too. You look at different industries when you do that, too. Now, I can't tell you that the net comes out so that there is not some of those costs imposed, obviously.

But what I can say is that the SEC really does a very thorough analysis of cost-benefit.

Mr. FITZPATRICK. In terms of the size of the companies, a lot of the pharmaceutical and biotech companies don't have a lot of employees. They are highly compensated employees, and they may have a lot of market value, but they are not going to have any revenue for 10 years.

It could take $1 billion in research to get a therapy to market, with no profit until that point in time.

So what does the SEC cost-benefit analysis say about those companies, which are very important to my district, because they can't grow—they are spending money hiring external auditors, complying with a rule that I am sure was well-intentioned, but not intended to be impacting firms like these.

Ms. WHITE. I don't know how to answer that other than to say that our economists try to look at it not just as, here are the compliance costs, but what does it do to competition, what does it do to the other economic impacts besides just—and I don't mean to minimize it—the compliance costs.

But again, obviously, what is driving that analysis in the first place is a need—a perceived need, certainly, for some regulation to protect investors and the markets and to facilitate capital formation.

But we should be doing as deep a dive as we can, no matter what the industry is, no matter what the complexity—or uniqueness, maybe, is a better word. And I appreciate that is how the pharmaceutical R&D works, in particular.

Mr. FITZPATRICK. Thank you. I yield back.

Mr. DUFFY [presiding]. The gentleman yields back. The Chair now recognizes the gentleman from Georgia, Mr. Scott, for 5 minutes.

Mr. SCOTT. Thank you very much.

Chair White, are you aware that when we wrote Dodd-Frank, in Section 913 we gave exclusive responsibility to the Securities and Exchange Commission if there came a time when we needed to put together a best interest standard for the fiduciary? You are aware of that, aren't you?

Ms. WHITE. I am certainly aware that 913 gives the SEC authority to proceed. It doesn't mandate it. Yes.

Mr. SCOTT. Let me ask you this: why are you allowing the Labor Department to take over your territory that we put in Dodd-Frank, that was approved by the House, approved by the Senate, and signed by the President of the United States?

Ms. WHITE. I don't view it—and I have heard your comments before—that way. Again, we are separate agencies. They do have responsibility and statutory authority in the ERISA space. Even as we—

Mr. SCOTT. Let me—

Ms. WHITE. —sit here now, brokers have to comply, if they are in the ERISA space, with the Department of Labor rules and ours.

Mr. SCOTT. Let me respond to that, please. I was here. I helped write Section 913. There was a reason why the Securities and Exchange Commission came to set and let us do this—because they were the regulatory agency.

Now, you mention ERISA. Not once—not one time—did the Labor Department come over and said, "Hold on, let us handle the retirement." No. There was no discussion of that. That is just happening now.

This is a critical issue, and if there ever was a time for the Securities and Exchange Commission to stand up and do its duty so that all of the American people can receive the proper financial advice to make those critical decisions—do you realize what the Labor Department is doing?

Do you realize what position that is putting FINRA and you in as far as complying with these complexities? And if you allow that, and sit back and disavow the authority we put into 913, that would be a very, very serious indictment on the Securities and Exchange Commission.

So what I am asking you—and this is why—when you allow, and you pass a rule which says that instead of a Commission base, that now you have to pay up-front, fee-for-service, out-of-pocket, before a financial investor can even talk to you about it, that has a clear, disproportionate impact on the lower income, the middle income, and especially African-American investors and other minorities, because they are not going to—they don't have that much.

And when you get to what they basically do—even if you get to the annuities, which is what they really utilize—but you have three different ones. You have the fixed annuity, the variable annuity, the indexed annuity. That in and of itself is enough to run most people away.

And then, if they go through that, then they have to sign a contract. Now, I tell you, Chair White—I want to ask for you to get more aggressive here. And because you are going to be placed in the middle, FINRA is going to be placed in the middle.

And if they had this unworkable best-interest contract exemption, it would result in low- and middle-income people being pushed from these less expensive Commission-based accounts to the more costly fee-based up-front out-of-pocket accounts.

How do you see FINRA managing this conflicting compliance obligation? Because under current regulations, FINRA must find cost to be a pivotal issue when assessing and making the difference between what is best here.

Our financial system is complex and complicated, and you are going to push out lower- and middle-income people from being able to invest with their retirement.

I have great respect for you, and I want to make it plain: Seize your authority back on this fiduciary issue. The Labor Department should have said, if we got a retirement, it is written in the Dodd-Frank, that the SEC has this responsibility. The respectful thing for them to do is at least come to you and FINRA, and say, let's harmonize something to address this.

This is not theirs alone, and I am speaking for an awful lot of very, very important people, the low income, the middle income and most African-Americans, they need you to stand up on this.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Georgia, Mr. Westmoreland.

Mr. WESTMORELAND. Thank you, Mr. Chairman. And thank you, Chair White, for being here.

Chair White, you realize that one of the things that we are responsible for is trying to help our constituents solve problems, and

I have one that I would very much like for you to address on behalf of my constituent.

Do you know what a naked option stress analysis is? Or an NOSA?

Ms. WHITE. I do now, I believe.

[laughter]

I think your staff indicated you had this issue with a constituent.

Mr. WESTMORELAND. Yes.

Ms. WHITE. I knew before, too, but I know more now than I knew before you had the question.

Mr. WESTMORELAND. You and I both know more about it than what we used to. And my constituent is, very, very aware of it, and he has been quite successful in his career. And it is a—the NOSA is a vehicle, created by Merrill Lynch to mitigate risk from naked options trade, and when it is triggered, the account holder must post an NOSA margin to cover potential losses.

My constituent has contacted me, and we have been over and over and over it with the SEC and Merrill Lynch and others, trying to find out what triggered this call. And he has been unable to get that resolved, and even though he has asked Merrill Lynch on several occasions to give him that, they said that is a resource that they have trademarked.

Now, do you think is necessary, do you think it is okay that a company like Merrill Lynch could patent something to use on their investors, and not be able to tell them what that is?

Ms. WHITE. I don't want to speak about the specifics until I know all of the specifics, but clearly there are a number of obligations with respect to this, disclosure obligations, suitability obligations. What I would suggest on this is that I—it sounds like you have been talking to the SEC, I don't know to whom at the SEC, but if I could have one of my senior staff people follow up with your staff member, let's see if we can get to the bottom of it.

Mr. WESTMORELAND. I appreciate that, Chair White, and I have a pretty good file here that I will get to your staff before you go, but it would certainly be something good, because this gentleman has jumped through all the hoops, and done everything, he and his wife both, to get an answer and have been unable to do that.

And so, any help that you could you give us as far as getting an answer or a conclusion of this, it would be much appreciated by me and Mr. and Mrs. Denny.

So, thank you very, very much, and I yield back.

Chairman HENSARLING. The gentleman yields back. The Chair now recognizes the gentleman from Texas, Mr. Green, ranking member of our Oversight and Investigations Subcommittee.

Mr. GREEN. Thank you, Mr. Chairman, and thank you, Madam Chair, for appearing today.

Madam Chair, I would like to get some things for the record; these are things that are of common knowledge to a certain extent. It is true that you are a member of FSOC, correct?

Ms. WHITE. Yes.

Mr. GREEN. And that as a member of FSOC, you have voting privileges?

Ms. WHITE. Yes.

Mr. GREEN. And that as a member of FSOC, which is a newly formed institution as a result of Dodd-Frank, you have the ability to look at the entire financial system, looking for risk that may be out there that can hurt the system, is that correct?

Ms. WHITE. Yes.

Mr. GREEN. Simple terms.

Now, in doing this, Madam Chair, would it be fair to say that if we had had FSOC prior to 2008, we all would have been more likely to see the risks that AIG posed, than less likely to see them? Is it fair to say that there is a greater likelihood we would have seen some of these concerns with AIG?

Ms. WHITE. It is always hard to judge that, obviously, and that you see what you see. But this is a mechanism that is enormously important to seeing risks as early as possible, because you have to bring all of the relevant financial regulators, or a good component of the financial regulators from different strata, in a room together, to talk about what they are seeing. And there is no real substitute for identifying a problem early than that, I think.

Mr. GREEN. This is why I ask in terms of more likely or less likely. More likely to have seen it or less likely?

Ms. WHITE. Certainly in theory, it should be more likely.

Mr. GREEN. And in reviewing entities such as AIG, which had this London office that was doing some things that we didn't find quite acceptable after the fact, in reviewing these things, do you spend an inordinate amount of time at entities that don't come under the $50 billion threshold as a trigger, or designation as a SIFI?

Do you spend a lot of time before you cast that vote?

Ms. WHITE. You spend a lot of time before you cast a vote, a lot of time.

Mr. GREEN. And do you have an office to help you with research, the Office of Financial Research (OFR), to help you with the research? People who provide expertise to the Treasury, and the Treasury can share its—

Ms. WHITE. And certainly, OFR does research on various issues. The FSOC staff, and the staffs of the member agencies also do a lot of work.

Mr. GREEN. Thank you. And when you cast your vote, are you told how to vote? Or does someone say to you, you have to vote a certain way on these issues?

Ms. WHITE. No.

Mr. GREEN. Is it your opinion that you have been a pretty independent person serving on this FSOC?

Ms. WHITE. Yes.

Mr. GREEN. And as an independent person, you put your time in and you study things, and you come to final conclusions?

Ms. WHITE. Yes, and I studied it with, not only the FSOC staff, but our staff.

Mr. GREEN. Now, I just looked at some of the information on some of the very large companies in this country. A good many of them have triggers that bring them under the auspices of the FSOC and the SIFI designation. If you have to study every one of them to ascertain whether or not it should be a SIFI, it would take a lot of time to do this, wouldn't it?

Ms. WHITE. No question.

Mr. GREEN. Do you have the personnel, such that you can study all of these mega-corporations that are $50 billion and above, do you have the personnel to look at them with the kind of detail that you need, if you did not have the trigger to bring some of them under an umbrella?

Ms. WHITE. Obviously, the resources are finite. You try to prioritize the ones that pose, potentially, a systemic risk.

Mr. GREEN. And do you find that it is beneficial to have a trigger, whether it is at $50 billion or some other amount, is it beneficial to have a trigger?

Ms. WHITE. That is a little hard to judge, because obviously, what we are presented with are those that have met that trigger. So you don't know what hasn't met that trigger, I guess, to some degree. But logically, yes.

Mr. GREEN. And without the trigger, you find yourself having to answer a good many more MetLife questions and a good many more questions that relate to entities that you are trying to sift through and ascertain whether or not they are SIFIs?

Ms. WHITE. I think it would depend on what substitute methodology you had.

Mr. GREEN. Okay, thank you very much. I yield back.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentleman from California, Mr. Royce, chairman of the House Foreign Affairs Committee.

Mr. ROYCE. Thank you very much, Mr. Chairman, and Chair White, thank you.

If we look back to the collapse of Lehman Brothers, one of the lessons was the need to quickly understand the relationship of corporate entities to one another. And so, out of the ashes of Lehman's downfall, came the Financial Stability Board's (FSB's) concept—and this was actually the direction of the G-20—this concept of legal entity identifiers, or LEIs, as we call them, where each entity has to register that unique 20-digit code, and that makes their identity very clear when you are trying to unravel something in real time, in terms of all their financial transactions.

So last month, this committee passed legislation, which I authored, requiring the Office of Financial Research to provide an annual update on the progress of adoption of these LEIs, here in the United States.

Now the global adoption I think is at 400,000; 400,000 LEIs now in 180 countries. So if the OFR were to conduct its report today, I am afraid that the SEC would lag behind a bit in terms of the adoption in other countries. As we move towards more transparency, this obviously this is part of our mission, and I think the Commission did mandate the use of LEIs in its security-based swap rules.

It didn't require it in other rules. So I guess I would ask, should we expect that the SEC is going to require greater use of this important risk management tool in the future?

And is there anything holding you back in that regard?

Ms. WHITE. There is nothing holding us back. If it is appropriate to the space, you want to make sure it fits, right?

But I think LEI is an enormously important tool.

The SEC has been a very strong proponent in those global efforts that you mentioned, and we frankly look for—we are looking for opportunities to use it more, I guess is the way I would answer your question.

Mr. ROYCE. But to get to that point, you might promulgate more rules in that direction in order to increase the adoption where appropriate.

Ms. WHITE. Essentially, as we are adopting whatever rules as we go forward, we would look for that opportunity.

Mr. ROYCE. Right. Let me ask you another question, Chair White, which goes to the Financial Services Committee's focus here under the chairman. What we have been trying to do, under the chairman's leadership, is to take a strong interest in housing finance reform and see how we can move forward the concept of bringing more private sector credit risk sharing into the GSE's. We would like to get as many positive things done as we possibly can in this quarter.

So real estate investment trusts are a logical investor in these transactions. We have seen the communication from the FHFA which says that it does not perceive any drawbacks from greater involvement by REITs in credit risk transfers. This might be an area that, sooner rather than later, we can move forward additional steps to get more private capital. Could you work with us to clarify that all of these risk transfer deals are viewed as good read assets that do not undermine investor protections?

Ms. WHITE. We certainly would be happy to work with you on that, and I think the staff may be working with you on that, but I will make sure that they are.

Mr. ROYCE. I think that would be helpful. I think it is very clear that as the Federal Housing Finance Agency says, at the end of the day, there is a clear benefit in getting credit risk transfers to get more private capital back in here for this part of this equation and that REITs can do this, according to them, and according to us.

We certainly see the benefit to this and it is—when you are looking at a significant source of private capital like this, it just doesn't make sense to, just because regulatory hurdles, prevent that capital from being deployed. So we would appreciate that assistance.

Chairman HENSARLING. Does the gentleman yield back?

Mr. ROYCE. Thank you, Mr. Chairman.

Chairman HENSARLING. The gentleman yields back. The Chair now recognizes the gentleman from Washington, Mr. Heck.

Mr. HECK. Thank you very much, Mr. Chairman. And Madam Chair, thank you so very much being here.

I want to ask about the Volcker Rule, which I consider to be fairly important. Of course, the Rule is final, but it is not yet being enforced and is, at the end of the day, I guess rather a bit of an experiment. So I want to pick your brain a little bit about it as we await the time when it is actually implemented.

What are you saying in terms of market behavior and anticipation of the effective date? How do you see the market changing? How do you see companies adapting to it? And do you yet perceive any change in the risk being taken in the risk to the financial system? Just talk generally about those kinds of things. Is that—

Ms. WHITE. Again, it is a little hard to judge at this juncture with certainly, with any definitiveness on that. We are basically just about now going into the exam for the compliance period, actually, and all the agencies are.

We are coordinating well. We will learn more from that, but before that period actually kicked in, we were obviously talking to those subject to the rule to see if they were able to provide the metrics they needed to comply and really, they got a very—at least initial, positive read on that.

Mr. HECK. What does positive read mean?

Ms. WHITE. Positive read, meaning that they should be able to comply in a timely way. Now obviously, there are exemptions in the Volcker Rule and there are prohibitions in the Volcker Rule. And compliance is really at the trading desk level, and so there is a lot to look at in terms of is this market-making, or is this something that is prohibited?

I think we have to see what comes out of certainly this first wave of exams to see, is it working, is there good compliance, and then in terms of judging its effects, I think that is down the road a bit.

Mr. HECK. But where you sit here today, based on what you know and given that it is limited, are you confident that it will in fact reduce risk to the financial system?

Ms. WHITE. That is certainly the objective, which is basically to not have these institutions that are connected elsewhere engage in proprietary transactions. But again, I am a person who likes to wait on the data, but I think that is certainly the purpose.

Mr. HECK. It is the purpose. Are you confident that it will achieve the purpose in large part?

Ms. WHITE. I have to see the data. I am afraid on that.

Mr. HECK. Okay. Subject two. You are also currently reviewing a change in definition for accredited investors. Your predecessor was pretty clear that it very much needed to be changed and updated. So I would like to ask you what the status of your review of the definition of accredited investor is, just a general timeline for you think that—where that work will end up, what you personally think the direction needs to be.

Ms. WHITE. Sorry.

Mr. HECK. Go ahead.

Ms. WHITE. First, clearly it, for a while, needed a really deep dive look in terms of all the various criteria that needed to be considered, not just net worth and income levels, but including them.

Our staff has been studying that quite intensively for some time and they really are coming to a conclusion of their work.

And the next step—really quite in the last phases of that and the next step, which I think will be relatively soon, I know you will want me to define that next, but relatively soon to basically put out publicly what those findings are and what the analysis is.

Mr. HECK. Is "relatively soon" something like 90 to 120 days?

Ms. WHITE. I would think so.

Mr. HECK. And do you personally believe that there is a definitive need to update?

Ms. WHITE. I do believe there is a definitive need to update. I can say that much. Yes.

Mr. HECK. Can you give an example of the kind of change that you think—

Ms. WHITE. I don't want to get—again, we will have to decide this, so I don't want to get ahead of when we are a five-person Commission also. But clearly, what we are looking at beyond the traditional tests of net worth and income, are other kinds of sophistication, experience, qualifications that certainly many, many would argue should entitle you to be an accredited investor.

And I think one wants to be sophisticated about and realistic about what those other criteria are that would meet any investor protection concerns, frankly. So we are looking quite broadly.

Mr. HECK. Thank you. With that, I yield back the balance of my time, Mr. Chairman.

Chairman HENSARLING. The gentleman yields back. The Chair now recognizes the gentleman from Virginia, Mr. Hurt.

Mr. HURT. Thank you, Mr. Chairman, and I thank Chair White for appearing before us today.

In your testimony, you touched on equity market structure. I wanted to highlight one of the things that you said. You said that you all had been proceeding, since your last visit here, with an ongoing assessment of the U.S. equity market structure to ensure that our markets remain the deepest and fairest in the world and optimally serve investors and companies of all sizes seeking to raise capital.

I wanted to turn your attention to the national market system plans, NMS plans, that were created in 1975 as an amendment to the Securities Exchange Act 40 years ago, and obviously a lot of things have changed since that time. The U.S. equity exchanges at that time were not-for-profit; they were member-owned. Today, of course, they are publicly traded and they are for-profit. And so a lot has changed in the last 40 years.

When you talk about plans for the collection and dissemination of market data, I think that we would all agree that if you want to ensure the deepest and fairest markets in the world and optimally serve our investors, you have to have accurate market data, and that has to be collected and disseminated in a fair and accurate way.

In the aftermath of the of the NASDAQ SIP outage in August 2013, I think there were some concerns that were raised about the governance of these National Market System (NMS) plans. We know that the NMS plans—plan participants are exclusively representatives of the exchanges in FINRA with no industry representation, and that leads it—it has been argued, to two separate problems.

One is that you don't have a broad-based representation among these participants in providing the best sort of leadership and vision for what needs to take place in making sure that these SIPs are the best they can be.

And then two, and perhaps of greater concern, is the conflict of interest issue, and that, of course, has to do with the fact that because the way the revenue is shared, there is a disincentive to invest in the SIPs to make them good as they should be.

And also, the secondary issue relating to a conflict of interest has to do with the fact that these exchanges have their own data feeds that compete the SIPs information.

So I was wondering if you could talk a little bit about where you are, and what you think can and should be done as it relates to the reform in the governance of these NMS plans?

Ms. WHITE. This is one of the reasons that I correctly identified this very deep comprehensive review of NMS and equity market structure, even before I was confirmed, as one of the highest priorities, and we have proceeded on that really, in a sense, on two parallel tracks. One, there are some things that clearly would optimize the markets that we are proceeding on in terms of specific rulemaking.

And then the other is really the more comprehensive review. That takes into account—and we have obviously spent a lot of time dealing specifically also with SIP governance and single point of failure and it is enormously important that the SIP provide its information quickly with the consolidated information.

And we are—and I think you can see, from our work on the Market Structure Advisory Committee and the subcommittees that we just formed, that we are looking very much at that issue—those issues, as well as just kind of the whole role of the exchanges in the equity market system. We are not—we haven't concluded on those things, but very much front attention.

Mr. HURT. Can you, as you sit here today, explain to me what resistance there is or why we should continue to have these participants that are exclusively from the SROs, without including anybody from industry?

Ms. WHITE. I am not sure I can provide that answer, other than to say that one of the things we need to make sure of as we are making the changes, is that the system continues to function. And I am not suggesting putting a representative of the industry on there; that would mean it didn't continue to function, but we are trying to sort of optimize every aspect as we go.

So, I could probably provide you some further information on that.

Mr. HURT. I would appreciate it. And I do think that the conflict of interest issue is something that obviously goes to the fundamental fairness issue that I think that we all want to see in our markets.

Thank you. I yield back.

Chairman HENSARLING. The gentleman yields back.

The Chair now recognizes the gentleman from California, Mr. Sherman.

Mr. SHERMAN. Thank you.

I bring up FASB's $2 trillion addition to the liabilities in assets on American balance sheets each time you are here. I want to commend you for stepping forward—and say yes, FASB gets their authority from the SEC, and you take responsibility for their decision to delegate that authority.

They didn't follow the Administrative Procedure Act. They didn't listen to anybody in the construction field. They didn't do any cost-benefit analysis. And we are going to see a decline in construction employment as a result of this new rule.

So I will just ask you: Do you take responsibility for all that?

Ms. WHITE. We have had this discussion before. And again, the SEC has ultimate responsibility for accounting standards. We have obviously, for many, many years, recognized the private sector, therefore FASB is the standard-setter. And the SEC has the power—

Mr. SHERMAN. And if I can interrupt, the SEC hasn't required them to follow the Administrative Procedure Act. The SEC has done nothing with regard to their processes or their outcomes.

Ms. WHITE. I understand your point. From your point of view, they haven't followed their due process procedures. I certainly haven't received that information from any other quarter in terms of the process that they have followed.

Mr. SHERMAN. You haven't received that information from whom?

Ms. WHITE. Among others, obviously people comment on their process publicly all the time, as well as our staff and the Chief Accountant's office.

Mr. SHERMAN. The people who comment live in the world I used to live in—the world of accounting. They have barely heard of the Administrative Procedure Act. It is foreign to that world to let carpenters and pipefitters come before the agency and say, "Please don't ruin my family and my job." And so they refuse to listen to any of those people.

Ms. WHITE. Again, information that is coming to me is that FASB—comments were received on this proposal obviously several times. And that they were responsive to some and not to others.

Mr. SHERMAN. They wouldn't—that is why I am using the word "listen," rather than the word "invite" people to send e-mails that will be thrown away. They wouldn't listen to anyone. They didn't do a cost-benefit analysis. We are going to see a decline in construction jobs. There is no benefit from this—

Ms. WHITE. Of course, the standard is meant obviously to convey the economic reality of the transaction. And I know we have had this conversation before, but it was actually in 2005 that the SEC staff recommended that FASB undertake the, in effect, capitalization of—

Mr. SHERMAN. Right, with no cost-benefit analysis; they never discussed it with anybody who showers after work rather than before work.

Ms. WHITE. And, again, in terms of where a cost-benefit analysis comes in or doesn't for an accounting standard, because the purpose—I know you are a CPA, and a very good one, but the purpose is really to convey the economic reality of the transaction. I know they put off the transition period. We are cognizant of—

Mr. SHERMAN. Right. The transition—they don't convey economic reality in their discussions, which is why they have no defense for FASB number two, which also distorts the American economy by penalizing companies that engage in research.

Every accounting—and I will ask your Chief Accountant to look at this because it is proof that they don't always do it on the basis of economic reality—theorist for decades has said that you capitalize research. They don't, because it is not convenient.

And to come here and say, well, they just reflect accounting theory and economic reality, is a misstatement of what they do. And I know I have brought up with your people FASB number two, and they basically say, "Look, we don't want to listen to reality; we don't care; we want to do what is convenient."

And this approach—if the same people who tell you that accounting theory—and it doesn't—requires leases to be capitalized, let them cite you any accounting theory which says that research should be written off and not capitalized. The accountant—you have empowered. You take responsibility for. They give you some talking points. These decisions are as important as any reached in Congress.

They affect hundreds of thousands of lives. And the procedure and the outcome is not something that your agency can be proud of.

I yield back.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from South Carolina, Mr. Mulvaney.

Mr. MULVANEY. I thank the chairman.

And thank you, Chair White, for coming in today.

A couple of minor deals, and I am going to talk more than I ordinarily do, just so we can have you understand where we are on a couple of different things.

Thank you very much, by the way, for offering the proposed regulations on crowdfunding. The last time you and I spoke in March, you gave us your best efforts to get them done by the end of the year and we appreciate that. I understand they were published at the end of last month, the end of October, and they are out now for review.

When can we expect those to be implemented on the JOBS Act, the crowdfunding portion of that?

Ms. WHITE. Essentially—I think they become effective in, I want to say October 2016. They are final rules now.

Mr. MULVANEY. Right.

Ms. WHITE. So it is a matter of the effective date. I think it may be October, but it may be earlier.

Mr. MULVANEY. Okay. So, October of next year or earlier.

Ms. WHITE. Yes, but I think it could be May. I will have to give you the exact date.

Mr. MULVANEY. That is fine. That would be great.

The only thing—when I got them, one of the questions I had was—I used to run a small business. They are almost 700 pages, which I suppose on the one hand is to be expected, given what we are doing here, which is going out to the retail public, small investors for the first time, so there are a lot of protections that need to be built in.

One of my questions, though, on this is how do you all—have you all talked about how you are going to handle de minimus violations? We have small mom-and-pop organizations—that is who this is designed to help—now having to deal with 700 pages full of regulations. Have you all given this much thought as to how you reconcile those two things?

Ms. WHITE. Look, the answer is we are not out there to get people on this. We want this marketplace to work; we obviously want investors protected in the marketplace. One of the things that I have done since I have been here on these new marketplaces that we are setting up, whether it is lifting the ban on general solicitation or A+ or crowdfunding, is to have an interdivisional working group all over it when it begins, as opposed to looking at it a year from now.

Which means, as part of that, it is not just Enforcement or Examination, although it includes that clearly. But it is also Corporation Finance and Trading and Markets and people who can give guidance and help people conform to the regulations as we go. So hopefully, that will be helpful.

Mr. MULVANEY. And lastly, and just—

Ms. WHITE. The effective date, I happen to have here.

Mr. MULVANEY. Okay.

Ms. WHITE. Once in a while, I bring a piece of paper: May 16, 2016.

Mr. MULVANEY. Beautiful. Thank you for that.

Lastly, you all changed the size of the investment for the small retail investors. You took it down to $2,000. Very briefly, could you tell us your thinking on that?

Ms. WHITE. What we were doing in the crowdfunding space was to try to address concerns. We got comments from both directions, such as, this is just not going to be workable; there is not enough capital. You are sort of shutting people out of the markets, too. We really are concerned about fraud, and people losing money.

And so that was one of the adjustments we made in respect to comments we got—really, in direct response to comments we got.

Mr. MULVANEY. Thank you. I encourage you to keep an open mind. If things work out as we hoped they would when we passed the bill, then we can review those limits as well as other things in the bill.

I want to switch gears now to the Small Business Credit Availability Act that Ms. Waters mentioned in her comments. And I am going to speak more than I am going to ask here, just to let you know where we are coming from on a couple of different things that are in this bill.

So, we are talking now about BDCs. We have your most recent letter from early November. We have gone through it. And we are very excited about working with you to get the SEC okay with it. I think you know that we have worked with your folks over the last 18 months to do exactly that.

You raised a couple of things in your letter that we think are probably not entirely accurate, specifically dealing with preferred stock. In fact, we actually think that the bill does exactly what you say you want it to do. We look forward to sitting down with you on that.

There are other places where we think that maybe your concerns are a little bit misplaced. You have concerns, for example, about leverage and the impact of that on a retail investor. And we thought we had mitigated that by having that cooling-off period, by having the BDC announce they were going to lever up in order to give folks time to get out of the investment if they were uncomfortable with that.

So we think we have addressed some of the other things.

Regarding the 1 year, I know you objected in your letter to only having 1 year to write the rules. Keep in mind, that grows a little bit, Chair White, out of our experience. As happy as I am that we now do have the JOBS Act crowdfunding things, they are almost 3 years late. And so we are sort of trying to hold your feet to the fire, as we do as Congress.

Secondly, we do think that a lot of the changes that are contained in the bill are not going to require very dramatic changes in the rulemaking. It could be as simple as changing ratios or changing numbers and so forth without doing a wholesale of review. So we hope that when you sit down to do the rules, you will see that maybe it will be easier to write these rules than you anticipated in your letter.

Finally, and this is the big one, I hope that—when you first looked at it back, I can't remember, it was October, you didn't have a problem with a couple of different sections, specifically section 60 of the bill, when you said, in your view, these provisions did not raise significant investor protection concerns. In the most recent letter, you say the exact opposite about the same section.

So we do hope that when we do sit down, we won't have a circumstance where the goal posts moved, and we can simply work on it together.

Ms. WHITE. It was based on experience in between, but we are happy to work with you and your staff.

Mr. MULVANEY. Thank you very much.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Minnesota, Mr. Ellison.

Mr. ELLISON. Thank you, Mr. Chairman.

Chair White, conflicted investment advice costs investors a lot of money. Some have said $17 billion a year. And I am very concerned that workers who are sold IRAs with high fees and hidden commissions damage their retirement security. And I am very supportive of the Department of Labor's decision to move forward with a rulemaking to protect workers.

The SEC and the DOL have different jurisdictions, statutes, missions, and mandates. For example, the SEC does not have authority over insurance. I would prefer the SEC follow the lead of the Department of Labor in protecting the retirement accounts of workers.

So can you respond to that? I would like to know what your thoughts are on this issue. Do you see there being a looming retirement crisis? And what role would a "best interests of the consumer" standard be, and what value would that be in terms of moving forward in this space?

Ms. WHITE. My own personal conclusion—as I think I surely have conveyed before—is that we should subject brokers and investment advisors to a uniform fiduciary duty based on the Section 913 recitation of best interests of the client, irrespective of your own financial interest.

And that obviously applies to those classes of registrants. In terms of what the Department of Labor is doing, I have said before, they are a separate agency, they have separate statutory authority, and they are proceeding.

Obviously, coordination is important. We do that with all kinds of agencies when there is some overlap. From our point of view—my point of view, and again, it is up to the entire Commission as to whether and what the parameters would be of our uniform fiduciary duty role—it would be done under Section 913 of Dodd-Frank, which, as you know, provides some parameters to our uniform fiduciary duty that takes some specific cognizance of the broker model, I think.

And so that is one of the things that we would obviously have to be considering as we proceed under that authority, which is different than Labor's authority.

Mr. ELLISON. Thanks.

Also, when you were here in March, I urged you to finalize the CEO median worker pay ratio rule. I'm glad to see that the SEC has finalized that rule. Congratulations, and thank you.

The gap between CEO and worker pay has grown substantially, as you know—from 20 to 1, back around 1980, to now 300 to 1, which is really remarkable.

Now, most people come at this from a moral standpoint, and they say it is not right and it is not fair, and I agree that they are right. But I want to ask you about something a little different. Is it good for the economy at large?

And so, I would like to direct your attention to a graphic that I have. Many argue that paying CEOs in stock options encourages them to prioritize their personal short-term benefit over long-term needs of workers, investors, and the firm.

Many have called to eliminate the CEO performance pay loophole in Section 162(m), because stock options are considered performance-based under Section 162(m), the deductibility is unlimited. Do you have any thoughts about this?

Ms. WHITE. I speak as the Chair of the SEC here. I think one of the things that we have been very active in is disclosure of executive compensation.

And indeed—we talked a little bit earlier about Section 956 in the Dodd-Frank Act, that we and fellow regulators are working very hard on, which is basically incentive comp, to make sure that excessive risks aren't taken.

I think I have to leave to others, the broader issue. So that is really not in our remit, as they say.

Mr. ELLISON. Yes, but do you agree that—I am sure you are well aware, when people talk about the disparity between CEO pay and median pay, a lot of times the argument is, is this right or not.

Leaving that argument aside, do you have an opinion as to how a very wide disparity—say, going from, say, 20 to 1 in 1980 to 300 to 1 like nowadays—how does that impact the functioning—the proper functioning of markets, of retirement, of consumer demand? Do you have any views on that?

Ms. WHITE. I think where we operate in that space—if we do, in particular—would be in the 956 space, which is basically to try to ensure that the incentive compensation of executives—oversimplifying a little bit—in financial institutions is not done in such a way as to encourage excessive risk-taking, which obviously—

Mr. ELLISON. That is what I am asking you. Do you think it does?

Ms. WHITE. We are going in our rulemaking with our fellow regulators, we try to deal with that.

Mr. ELLISON. I appreciate your answers.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentleman from North Carolina, Mr. Pittenger.

Mr. PITTENGER. Thank you, Mr. Chairman. Good afternoon, Chair White.

Chair White, in your opening statement, you clearly conveyed that you are committed to the three-pronged statuary mission—to protect investors, maintain fair and orderly and efficient markets, and facilitate capital formation.

Included in that, do you read anything that would be considered social engineering?

Ms. WHITE. I wouldn't, no.

Mr. PITTENGER. Yes, ma'am.

In that light, over the last 5 years, you have spent thousands of man-hours and millions of dollars to defend rulemakings that really don't address the crisis and, from our perspective, don't fit into the scope of your mission, whether you are dealing with the conflict minerals issues or the resource extraction or the CEO pay disclosure rules that were just discussed.

How do you relate your role in these issues—it seems to me to be a diversion, whether—in terms of scope of mission. Is this an interest of yours? Is this something of the Administration that you feel compelled to carry? Why would you move away from what clearly is your scope of mission?

You are coming and you are wanting to increase your budget by 25—at a billion and a half right now, to go to billion eight—.88. A significant amount of money, and it seems to me that it is expansion of your footprint. It is expansion of your role and expansion—the bureaucratic entrenchment of your agency.

As we look at the Federal Government today, people are concerned—they see the overreach, they see the footprint of the Federal Government. They see the impact. Look at our economy. A very slow economic growth of 2 percent.

Do you appreciate the fact that maybe this death by 1,000 cuts in terms of overregulatory involvement of the engagement in so many of these unrelated efforts having an adverse effect that may be well intended, well designed by those who share those concerns, but killing the goose that laid the egg?

In trying to protect everything, aren't you hurting the overall cause?

Ms. WHITE. First, I very much believe in furthering our core tripartite mission, and I think I have talked about that at some length, and it has several aspects to it.

I think what you may be alluding to, at least primarily, are some of the congressional mandates that the SEC was charged by Congress—and it is Congress—to carry out.

And what I said a little bit earlier is, I do believe, when I have a congressional mandate, that means I carry it out. We try as hard as we can to carry it out in as cost-effective a way—

Mr. PITTENGER. Do you feel as though—

Ms. WHITE. —and as consistent with our mission as we can.

Mr. PITTENGER. —Chair White, that fits into your scope of mission?

Ms. WHITE. It is part of the mission given to us by Congress.

Mr. PITTENGER. As you stated earlier, to protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation—do these extra additional forays really fit into that scope of mission?

Ms. WHITE. I think we can't talk about them as a group. We have obviously done a number of the mandates that you might put in that category, that we have certainly seen some investor advantage to. But again, if it is a congressional mandate, I think we have to—we have an obligation to carry it out in the best way we can.

Mr. PITTENGER. Let me ask you this in closing. If there are excessive disclosure requirements that hurt our capital markets, if that is true, and would you buy into that, that there could be?

Ms. WHITE. Part of what we are trying to do with the disclosure effectiveness review is to make the disclosures more meaningful for our investors and obviously not to create gratuitous—

Mr. PITTENGER. We are talking about an excessive amount. We hear from the market continually about the excessive burden of these disclosures. They increase the compliance cost, they make it more difficult to raise capital, all of these things have a combined effect to slow our markets and impact our economy. Would you agree that the reality is that these excessive burdens are really having an adverse effect?

Ms. WHITE. It is one of the reasons we do that very deep cost-benefit analysis I was describing before. We obviously want to look at—

Mr. PITTENGER. But let's look at the overall—

Ms. WHITE. Not burdening, but—

Mr. PITTENGER. Respectfully, I just have a few seconds left. Respectfully, can I say look at the results today, it is all about results. Can you say with all your good judgment, with all these disclosures, all these requirements, all these mandates, all these compliance issues have been healthy as it relates to growing and expanding our economy? Or has it honestly had an adverse effect?

Ms. WHITE. I don't think it is static; I think we have to be focused on as these rules go out that we think are important looking at exactly that.

Mr. PITTENGER. Thank you.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentleman from Florida, Mr. Murphy.

Mr. MURPHY. Thank you, Mr. Chairman. And thank you, Chair White, for being here. It's good to see you.

My first question, I think, was already somewhat asked by the gentleman from Massachusetts, Mr. Capuano, regarding Petition 4637 on the shareholder funds for political activities. Just to dive into that a little bit more, as far as timing for a response from that, where do you think we stand and what is the timing that you think we can expect to hear back from you?

Ms. WHITE. On the letter, you mean?

Mr. MURPHY. Yes.

Ms. WHITE. As I have said earlier, I have three relatively recent letters, some from members of this committee, another one from different members of this committee, and I am expecting to respond to them fairly shortly.

As I have also said, though, we are focused on our mandated rulemakings and mission-critical initiatives that I have described.

Mr. MURPHY. And just to make sure—my understanding is when 1.2 million comments put in that this is a record, I guess, just to make sure, you feel that is sufficient to move forward.

Ms. WHITE. There have been a lot of comments on this and very strong views on both sides. I think there are about 2,000 unique comment letters. There is clearly intense interest on both sides of this issue.

One of the things I mentioned before is that I watch what is happening in terms of companies—the shareholder petitions that are being filed, which is through our regulations that is made possible and the number of companies increasingly that voluntarily are making those disclosures. There is a recent survey out, I think, just in the last 2 or 3 days showing those numbers are up.

Mr. MURPHY. Okay. Thank you. And then as it relates to DOL and their moving forward on fiduciary duty, I know there have been some questions on that as well. Can you just elaborate a little bit more on the distinct responsibilities between SEC and DOL and how you plan on moving forward with this?

Ms. WHITE. Sure. Essentially two separate agencies, two separate statutory regimes. The Department of Labor obviously is responsible for the very important ERISA space and has been since 1974, I think.

And again, I think I mentioned this a little bit earlier, but actually even as it exists now, brokers for example who are our registrants who are in the ERISA space or parts of the ERISA space are subject to different DOL rules and different rules under the securities laws and regulations. So I think each agency has to judge for itself how it is proceeding.

With respect to the SEC, we don't have a mandate to proceed with the uniform fiduciary duty, but we have authority given to us by Dodd-Frank in Section 913 to do that. I personally, after lots and lots of study, made the judgment that I think we should proceed with analyzing a rulemaking to impose a uniform fiduciary duty consistent with Section 913. There is a lot of analysis to do on it, economic and otherwise, and it is complex and not a quick exercise.

I think the Department of Labor's initial proposal on theirs was actually in 2009.

Mr. MURPHY. Yes. I think one of the concerns we all have on both sides of the aisle is duplication, and multiple, multiple agencies are looking at the same exact thing. I know you have had some meetings with Labor Secretary Perez and hopefully I am sure having these conversations is your way of staying in your lane, and who is doing what.

I think we all want to get the bad actors out, but at the same time don't want duplication. We want taxpayer money spent as wisely as possible.

Have you had that conversation? Where do you see that heading?

Ms. WHITE. What we have done—and I think this is again before I was here, but really from 2009 forward—and then obviously I am familiar with the more recent context—is the staff of the SEC—this is not the Commission, although I also participated in some meetings with Secretary Perez—provided technical assistance and expertise from our space to them, some of our economists met with them on a number of the issues.

And I think, as you do in—frankly, any time you overlap with any other agency—take the CFTC on swaps and securities-based swaps, you each have your authorities. They somewhat differ sometimes, but you try to be as consistent as you can because obviously it is not good for market participants if they have two sets of rules that they have to comply with. But often, there are different markets, different statutory obligations, and so there is not perfect consistency. But it is very important as you go forward on anything that overlaps that you talk and try to do what you can to conform.

Mr. MURPHY. I am running out of time. But quickly, can you just talk briefly about what you think the SEC's role is in cybersecurity? To me, that is one of the biggest threats that is—

Ms. WHITE. It is one of the biggest threats and risks we all have, full stop. The SEC has three areas of specific, I would say, jurisdiction. One is we did, I think, in November of last year, our regulation SCI, which is security, compliance, and integrity, which essentially is a rulemaking with respect to our critical market infrastructures to raise the bar on the resiliency of their systems and report incidents to us when they—and others when they actually have them. Part of that is cyber.

We deal with the brokers and the investment advisors and their risks. We put out disclosure guidance and we stay as active in this spaces as we can. We also bring enforcement cases when people don't—

Mr. MURPHY. Thank you.

Ms. WHITE. —do what they are supposed to under our roles.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentlelady from Missouri, Mrs. Wagner.

Mrs. WAGNER. Thank you, Mr. Chairman. And welcome, Chair White. I wore my Kansas City Royals blue—

Ms. WHITE. I see it.

Mrs. WAGNER. —to make you feel welcome from your first 10 years growing up with the world champion Royals.

Ms. WHITE. But I am a Yankees fan, as I told you.

Mrs. WAGNER. I know. I know. I am a Cardinals fan.

Ms. WHITE. Okay.

Mrs. WAGNER. In following up on some of the questions that have been asked about the DOL fiduciary rulemaking, I do want to associate myself with my friend, the gentleman from Georgia, Mr. Scott.

In the SEC's absolute purview on anything having to do with the uniform fiduciary rule, and following up on what the chairman said, you talked at the last SIFMA annual meeting about this full out focus.

So what does "full out" mean to you? When can we expect a rulemaking?

Ms. WHITE. I want to make clear at the outset, this is my view: It will ultimately be a Commission decision. I have obviously given staff direction, and they are very, very actively working on it. It is complex; it is not quick, but we are working toward—in the very short-term the—most of the details of what the proposal would be.

Now that doesn't suggest that in 2 months, you are going to see a proposal. This is a long, complex exercise, and it has to involve the full Commission.

Mrs. WAGNER. It does, and I am glad to see that you are looking at a shorter-term rather than the longer-term, and obviously, you will need to come back before this committee and the Senate Banking Committee; you have to talk about alternative remedies to a uniform fiduciary standard that would address investor confusion, including simplifying of titles, and enhancing disclosure.

All of these things are things that I hope are part of this ongoing analysis.

David Grimm, with your Division of Investment Management, stated that further analysis still had to be done. What is the scope of analysis, and what do you anticipate is the timeline for completing it?

Ms. WHITE. Again, I cannot kind of overstate the complexity and the importance of getting this right, and part of that is clearly the very deep economic analysis that our economists will do as we are proceeding with that.

So, in terms of impacts, in terms of—for example, I think have said this before, if we ended up at the end of the day with a rule that imposed uniform fiduciary duty, but we deprived retail investors of reliable, reasonably priced advice, we would not have succeeded, obviously.

And so, our economists have a lot of work to do as we proceed with this.

Mrs. WAGNER. You are correct, we have to get it right, and I think the DOL proposal is 1,000 pages of wrong.

Can you tell us about your analysis, including a study of the impact of the DOL's proposed rule on investment advisors registered with the SEC?

Ms. WHITE. It would have impact, I think, on investment advisors as well as broker-dealers. What we did with the DOL proposal, though, was essentially, as I mentioned before, provided technical assistance to them, which included—from our staff and it is our staff who are providing how it might impact on investors and how it might, what the lay of the land is now in terms of how brokers operate, how investment advisors operate.

It really depends on—and obviously, the Department of Labor is taking in a lot of comments about impacts. And so it depends on how—

Mrs. WAGNER. Tens of thousands of comments. And in fact, we received a letter, I received a letter from Secretary Perez, stating that they were going to make no changes, no re-proposals, even prior to the public comment period opening up.

And I am very dissatisfied with this. I know you said that you are providing technical assistance, and in that quote before Senate Banking, you even talked about, particularly the lower end, which I care deeply about, in terms of customers' choice, access to products, and the cost of those products. I think that is absolutely key.

Do you have any concerns that some U.S. investors could potentially suffer based on the new fiduciary definition that the DOL is proposing?

Ms. WHITE. I don't want to comment on that specifically, other than to say that I think the Department of Labor—and certainly, our technical assistance included that concern as you proceed with any rulemaking, and we have it in proceeding with ours.

Mrs. WAGNER. I am just looking at a couple of examples, here, on how the DOL, I think, conflicts with securities laws. And I understand that DOL's fiduciary duty rule will require financial advisors to provide 1, 5, and 10 year projections on investment returns as part of projecting investment costs under the best interest contract exemption.

Does this potentially conflict with the Investment Advisers Act of 1940, especially its antifraud provisions?

Ms. WHITE. I would have to analyze that with my folks in the Investment Management Division, specifically. But what I indicated earlier is even now we have different roles in the ERISA space—it is different statutory authority that applies to our brokers, our registrants than the Federal securities laws require. But I am happy to get back to you on a specific one.

Mrs. WAGNER. I would like that—for you to take a look at that, and also just, with the indulgence of the chairman, take a look at the DOL definition and term on recommendation. It differs completely from the definition used by FINRA. So I am concerned about some of these differences and really reiterate that this is the FTC's purview through Section 913, and we would love for you to move as quickly as possible.

Thank you, Mr. Chairman.

Chairman HENSARLING. The time of the gentlelady has expired. The Chair now recognizes the gentleman from Colorado, Mr. Tipton.

Mr. TIPTON. Thank you Mr. Chairman. Chair White, thanks for taking time to be here today. You previously stated that the independence of the SEC should be respected, and noted your particular expertise in terms of dealing with a variety of issues. And, with that in mind, I believe it is important that we consider the Federal Reserve's work on mapping transactions within the capital markets, and many view this as an early stage to be able to have the Federal Reserve regulate much of the capital markets under the guides complex transactions.

Are you fully committed to making sure that the SEC maintains its position as the regulatory body?

Ms. WHITE. Yes. I think one has to recognize, though, that after Dodd-Frank, there were some reassignments of some things, and so we end up doing more things in consultation with the Federal Reserve by statute.

I am not saying that is bad, I am just saying—but the short answer to your question is yes.

Mr. TIPTON. Great. If the Fed does continue this policy with securities products and firms, if they are going to be regulated under bankcentric modes, what type of an impact will that have?

Ms. WHITE. It is hard to answer that in a vacuum, and I do think—and we have discussed in connection with asset managers and—our doing stress testing as we are required to under Dodd-Frank. One has to recognize that asset managers are different than banks.

And so that means that however you regulate, however you stress test, if you do it optimal is going to be different.

Mr. TIPTON. Yes, and I think that is actually part of the concern that we are seeing as some of this is being formulated, that we are going to see and that this seems to be the track that they are on. To be able to try and de-risk completely is going to impact some of the work that apparently you are trying to do in terms of being able to have some capital formation—access to capital because that is one of the big issues that we are hearing in our communities, simply for small businesses to be able to actually—to be able to reach out.

Do you believe it is important that the FSOC has decided to review activities and products in the asset management industry for systemic risk?

Ms. WHITE. Do I think it is important, you said?

Mr. TIPTON. Yes.

Ms. WHITE. I think it is a focus that makes sense. It really goes beyond asset management. I think I cited before the example of securities lending as one of those activities. Obviously, that is not just asset managers.

FSOC really is charged with looking for systemic risks and addressing them in the system.

They have certain authorities and—to deal with them if—but I think the pivot, at least for the time being, from a firm focus to products and activities, makes sense the SEC staff has been quite active in, I should say, the December request for comment on those.

I see their work as complementary to ours, but we obviously have been the primary regulator of the asset management industry for 75 years and we are proceeding with a regime of regulations that we think is important to do and makes sense to do, and that is completely independent from FSOC. I think what they are doing is complementary.

Mr. TIPTON. Okay. I appreciate your answer on that, but you—one comment that you just made in terms of going through and seeking comment. One of the concerns, obviously in my district and maybe nationwide, is small businesses. You have the Government-Business Forum on Small Business Capital Formation and the response from the forum comes out and you—what do you believe are some of the most specific issues that small businesses are talking about right now?

Ms. WHITE. There are a number of them. We actually have that meeting tomorrow, by the way, our annual forum is tomorrow morning. It is enormously useful. If you look over the years, a number of the recommendations from that forum, I am not suggesting all of them—that we have actually proceeded with.

Clearly, they result in a lot of interest in crowdfunding. There is a lot of interest in A-plus. One of the things we did, by the way, when we did crowdfunding, is that we also proposed to amend our Rule 147 and Rule 504, which really is addressed precisely at those small, in-State businesses that want more facility to raise capital.

And so, that goes beyond the JOBS Act. That is not something mandated, that is something that we are very excited about, as were, frankly, the North American Securities Administrators Association (NASAA) State regulators.

Mr. TIPTON. Great. I do think it is worthy of note that Pepperdine University did conduct a study and it said that 53 percent of the respondents—small businesses—believe that the current business financing environment is restricting growth opportunities, and 46 percent believe it is restricting their ability to be able to hire new employees.

So I would encourage you, as you are holding those forums, not only to listen, but to actually hear what they are having to say because these impacts—cost benefit analysis that you have been speaking are having a real impact.

And Mr. Chairman, I ask unanimous consent to submit a question for the record in regard to 10K filings on a lot of our mining industries and to be able to get a response from that.

Chairman HENSARLING. Without objection, it is so ordered. The time of the gentleman has expired. The Chair now recognizes the gentleman from Texas, Mr. Williams.

Mr. WILLIAMS. Thank you, Chair White, for being here. You talk of your support for small business. I am a small business owner, and you support the International Financial Reporting Standards (IFRS), and as you know, the IFRS does not allow the use of last in and first out accounting.

My concern is, if we transition from the current U.S. method of generally accepted accounting principles (GAAP) accounting to IFRS, the toll on U.S. businesses would be unsustainable, and frankly cause most of them to go out of business.

I think the number to be recaptured is somewhere in the range of $100 billion. Now, you have publicly stated that considering whether to further incorporate IFRS into the U.S. financial reporting system is a priority of yours.

The last time you were here, I believe you told my colleague, Mr. Barr, that your object was to get a single set of global standards. FASB and IASB have made attempts in the past to come to an agreement. Those efforts have always been unsuccessful.

I saw in comments I believe he made yesterday, that the Chief Accountant, James Schnurr, urged supplemental use of global rules for U.S. companies. Yes or no, do you have any comments on how that would work?

Do you agree with that? Do you agree that it should be supplemental?

Ms. WHITE. Mr. Stivers, actually, I think you said he made a recommendation to me—he also made a speech, I think last December, about that, and certainly I am quite interested in that.

Just to be clear, what I have said, though, is that I think the Commission, if we can, should speak again on this issue.

Mr. WILLIAMS. Okay.

Ms. WHITE. Just speak again. Not saying what that would be. And so, I think in terms of sort of the one high-quality global standards as a goal, I certainly favor that.

That doesn't answer all the details along the way. It doesn't for a moment suggest what the position might be for further application of IFRS—they obviously apply to foreign private issuers. Now, that is very different.

Mr. WILLIAMS. All right, thank you.

Based on those comments—he, by the way, also said there is virtually little or no support among U.S. companies for a wholesale change—do you still consider incorporating IFRS as a priority of yours? Yes or no?

Ms. WHITE. Again, I don't think I ever stated that as a priority of mine. My priority was to get the Commission to say where we are.

Mr. WILLIAMS. Okay. Is your inclination to adopt IFRS based on a desire to have one standard worldwide financial reporting system, or is it because you believe the IFRS standards are preferable to GAAP?

Ms. WHITE. That is not what I intended to convey. The SEC, some time ago, before I came in, by regulation, has allowed foreign private issuers to use IFRS without reconciliation.

But plainly, the convergence projects have gone where they have gone and not gone where they have not gone.

Mr. WILLIAMS. All right.

Ms. WHITE. And so, there are differences in the system.

Mr. WILLIAMS. In the case of last-in first-out (LIFO) inventory reporting, IFRS does not allow the use of LIFO. In contrast, the U.S. tax code requires the use of LIFO for financial reporting if it is used for tax purposes.

Effectively, then, the SEC would be making tax policy. Were you aware of this potential impact?

Ms. WHITE. I am aware of the impact, but I don't want to imply for a moment that I think it ought to be done, period.

Mr. WILLIAMS. Yes.

Ms. WHITE. But clearly, it has IRS and IRC implications.

Mr. WILLIAMS. Do you think you should be, effectively, setting tax policy?

Ms. WHITE. No.

Mr. WILLIAMS. Okay. Do you have a substantive position on the use of the LIFO inventory method?

Ms. WHITE. I don't. Obviously, the method under GAAP is the one that applies.

Mr. WILLIAMS. You realize, though, how destructive it would be to small businesses here?

Ms. WHITE. I am quite aware of the complexities of that issue, absolutely. All I want to make clear is that I think some of the positions that you are indicating were mine really are—I haven't concluded on any of that.

My only priority is to get the Commission to say where it is on some of those issues, not suggesting for a moment where that would be.

Mr. WILLIAMS. Have you consulted with the Treasury about this potentiality? And if so, is the Treasury comfortable with the SEC setting LIFO inventory—slash inventory tax policy?

Ms. WHITE. The answer is I haven't consulted with Treasury on this because it is not ripe at all to consult with them on it, not because it is not an important issue, if we were to reach it.

Mr. WILLIAMS. LIFO is an important—

Ms. WHITE. Very important.

Mr. WILLIAMS. —accounting method for small businesses.

Ms. WHITE. Absolutely.

Mr. WILLIAMS. And the recapture of $100 billion, as I said earlier, could devastate small businesses. It could cost jobs. So I appreciate your following through on that.

Ms. WHITE. Absolutely.

Mr. WILLIAMS. Thank you, Mr. Chairman. I yield back.

Chairman HENSARLING. The gentleman yields back. The Chair now recognizes the gentleman from Maine, Mr. Poliquin.

Mr. POLIQUIN. Thank you, Mr. Chairman, and thank you, Chair White. I appreciate it very much. I know you missed your opportunity to go to Maine this summer, but I know next year is another year, and you will make it—

Ms. WHITE. I am coming.

Mr. POLIQUIN. —your vacation, and spend as much money as you can. I appreciate it.

Chair White, the State of Maine has the oldest average age in the country. And Maine's second district, which I represent, comprising western central, northern and down east Maine, is likely the oldest district in the country.

In addition to that, coast to coast, there are 40 million Americans who live in rural areas.

Now in parts of Maine—and, I am sure, other parts of the country—when you are living in those areas, we often don't have internet conductivity. We have power outages all the time, even if we do have conductivity.

In addition to that, 41 percent of our seniors in this country, regardless of where they live, don't use the internet. So, I know your mission, in part, is to make sure our investors receive all the information they can to make sure they are protected in decisions that they are able to make.

Now, one of your own studies back in 2012, Chair White, indicated that 71 percent of investors, regardless of age, prefer to receive their reports from mutual funds and what have you, on paper. Right now, there is a proposed rule in your agency—30E-3—that you and I talked about back in August.

Ms. WHITE. Yes, we did.

Mr. POLIQUIN. And in this rule, if I am not mistaken, a mutual fund company can simply send a letter to a senior or any other investor saying, you are no longer going to receive your quarterly statements or your portfolio holdings or whatever it might be unless you fill out this form and send it back to us saying that you want to continue to receive those reports in paper form.

Now, what happens if the mail doesn't go through? Or what happens if you are on vacation in Florida and you live up in Madawaska, Maine, and the letter gets lost in a snowbank? Or what happens if you change locations and you are in between addresses, or for some other reason, you are away from home?

This is just not fair, in my opinion, Chair White. It is just not right. So, I think when it comes to—with all due respect—the mission of the SEC, that I know you are responsible for upholding, it makes a lot of sense to make sure that our investors have the option of receiving their paper financial reports unless they opt out. Otherwise, it is much too confusing.

Now, if someone decides to opt out, instead of opt in, that is all fine. So I am hopeful that you will commit to me today that you will retain this option, because that is—with all due respect—part of your mission.

Ms. WHITE. I can't commit to that, because we have an open period of comment until January on this. What I can say—and we talked about this to some degree on the phone—is that the proposal tries to address the concern. Although, again, we have a number of comments in the same vein as yours, which we are obviously weighing very seriously.

But in the proposal we have tried—the staff has tried to build in, it is not just sort of one letter that gets lost in the mail. Which I understand is a risk, don't get me wrong. But also, it would periodically, again, be solicited on the issues—so some of the problems that have been identified in terms of receipt and choice the proposal tries to address.

But I fully take your comment about switching the presumption, basically.

Mr. POLIQUIN. Chair White, my mom, whom I love dearly, is 87. She can barely use a cell phone—

Ms. WHITE. But again, she would have the option not to receive it by—she could get paper—but I fully take the concern. Yes.

Mr. POLIQUIN. I appreciate that very much. I have a very short amount of time left. I would like to morph, if I can.

Chair White, thank you very much. Our financial services industries is the envy of the world, and it gives all kinds of options to investors saving for their retirement or for the kids' education, and also, is the backbone liquidity to our economy that allows us to grow and raise capital and hire more workers.

I am very concerned, and you and I talked about this a little bit this summer, I believe, also about asset managers and pension fund managers and mutual funds be designated as SIFIs. And in particular, I know there has been a movement through FSOC and also some of the other folks who come before us, that you are starting to look at activities instead of asset size.

Now, I would like to ask you if I can right now, what activities are of concern to you, because if Mr. Hill and I manage a couple of different pension funds—mutual funds—and his performance is better than mine—

Mr. HILL. It would be.

Mr. POLIQUIN. It would be. Then my clients would go to his and the assets are not on our balance sheet anyway. They held it in the trust department down the street. So if something happens to me, it is no systemic risk to the economy or to the capital markets.

Ms. WHITE. And I think that is why you have seen the pivot to particular activities. One of the things we are dealing with in our separate, primary regulator space too, is liquidity risk management kinds of issues, just to make sure that—because in an open-end fund, you are entitled to get your money right away. Those kinds of risks.

I mentioned before, securities lending, which asset managers and other people not even under the SEC's jurisdiction may use and does that pose any risk. But there are no answers there. It is really just asking questions and I think it is good to ask those questions.

Mr. POLIQUIN. I will submit to you, Chair White, that there is no risk in the asset management business model to the economy and please look at that very carefully and make sure, with your position on the international regulatory bodies, that you make sure that we stand up for American asset managers when it comes to any regulatory issues with respect to your industry.

Thank you very much. Have a wonderful Thanksgiving.

Ms. WHITE. Thank you, you too.

Mr. SCHWEIKERT [presiding]. Thank you, Mr. Poliquin.

I now recognize the gentleman from Arkansas, Mr. Hill.

Mr. HILL. Thank you, Mr. Chairman. Madam Chair, thank you for being back before the committee and congratulations on a good GAO audit. I know that makes every management team smile when you get that. And also, congratulations on clearing up some of your 50 front burners; maybe you are down to 40 or so now.

I would like to start out by talking about equity market structure. I thought SIFMA wrote a very thoughtful piece last July, I think, in 2014 about their suggestions on equity market structure challenges that we have seen over the course of the past few years, including some of the references to this summer.

And you have now formed an Equity Market Structure Advisory Committee and a couple of comments about that I am concerned about. I would like to get your thoughts.

I understand they have subcommittees meet in private without any transparency on their policy recommendations. I would like your thoughts on that. And then, I noted that the overall membership in the committee didn't include NASDAQ, it didn't include the New York Stock Exchange, it didn't include a big retail broker-dealer, and I come from the retail broker-dealer space, so I am always concerned about the best execution, the promise that we make to do as our regulator to achieve best execution.

So I am concerned those entities are not involved in your Market Structure Advisory Committee. Could you respond to that, please?

Ms. WHITE. Yes, I would be happy to respond to it. First, the Commission—and it is really all five of us on the Commission, went through a very lengthy process of vetting and of trying very hard to diversify points of view and expertise on the 17-person committee, which is what it is by charter. And so there is an exchange, obviously represented on the committee.

There actually is, at it turns out, two other representatives who were formally actually at primary listing exchanges as well. There is a representative who represents the retail brokerage point of view, although we still keep looking at that. And we have clearly had requests for others to join.

One of the things that we have done, and again, this is something you just keep looking at because you really want that diversity of perspectives, is to structure that committee so that we get input from others from every constituency, whether it is retail brokers or it is NASDAQ or it is the New York Stock Exchange.

So each of the meetings, in effect, is a roundtable where we have NASDAQ, and the New York Stock Exchange, and so forth.

And the subcommittees, that is something that the other advisory committees use to great effect to just get things done, but they don't decide anything, and they are also able to open at least parts of their meetings, if they choose, publicly.

Mr. HILL. Let me urge you to open those meetings or parts of those meetings. I only urge you to make sure you get the full complement of those who want to participate in this process in the retail industry, and particularly, so you include exchanges, but to not have the two leading exchanges, NASDAQ and the New York Stock Exchange, represented strikes me as short-sighted.

Let me switch gears. Generally, in your experience—I know you have an enforcement and legal background and I have an investment management background, do you believe that retirement fund managers have the principal obligation of maximizing long-term returns for their beneficiaries and their plans? Is that a general thing you bring to the table, is a belief that is their primary objective?

Ms. WHITE. Maybe it is because of that legal background and the SEC's jurisdiction, you want to serve the best interests of your client is what you want to do. That is what your fiduciary duty is.

Mr. HILL. Yes, but I think if you have full discretion over an account and you are an investment manager, you have to act in their best economic interest, wouldn't you say?

Ms. WHITE. Yes.

Mr. HILL. That causes me concern about a recent decision by the Department of Labor, not the fiduciary standard, but Secretary Perez has recently encouraged and has given guidance to institutional managers that environmental, social, and governance issues are equal to economic return issues. We live in a world of underperforming of defined benefit plans that aren't fully funded, and yet, we have direction from the guy who is in charge of ERISA to look at other things besides economic performance.

Would you like to respond to that?

Ms. WHITE. Do I want to? Or—

Mr. HILL. We will, it is really—

Ms. WHITE. —would you like me to?

Mr. HILL. —so much fun to do it.

Ms. WHITE. I don't want to comment on his specific comment. I will say that I think what you, and it is a lot of my—but, yes. I think what you are trying to do is serve the best interest of your client. Obviously, you can have a client who says, "Look, I care about this, this, this, and this as you invest for me." That is really up to your client.

Mr. HILL. Yes, but economic return—we are not fully funded and economic returns are how we achieve that and I think the Department of Labor is way off track there.

Last question, you have some vacancies on the Commission, and would you commit to this committee that you wouldn't bring controversial elements up if you don't have a fully functioning Commission that has bipartisan members on it?

Ms. WHITE. Anything can be controversial. I think what—

Mr. HILL. True. But I mean any big, major issue follow on that we are working on. We are concerned that you are going to not have a fully functioning Commission with bipartisan appointees and we would like your commitment that you would be cautious about what you try to bring through the Commission without fully confirmed bipartisan appointees.

Ms. WHITE. I do think the work right now—there are four of us: one independent; one Republican; and two Democrats, and we are moving forward with our agenda. I think we can. I am going to take everything into account, but I do think we should proceed. I don't know how fast confirmations—assuming they occur, which I assume they will occur.

But you obviously sort of read your agenda as you go along.

Mr. HILL. Thank you. I yield back, Mr. Chairman.

Mr. SCHWEIKERT. Thank you, Mr. Hill.

I now recognize Mr. Rothfus.

Mr. ROTHFUS. Thank you, Mr. Chairman. And thank you, Chair White, for being with us today.

I just want to touch on the—some of the folks have been talking about the bond market—corporate bond markets. I wanted to ask a question about that.

Has the FSOC, again, of which you are a voting member, ever conducted any analysis of the systemic risk that could result from a lack of liquidity in the corporate bond market due to regulatory initiatives like the Volcker Rule, in Basel III?

Ms. WHITE. I don't think, as phrased that way. Obviously, the four or five of us who report quarterly to this committee do that kind of assessment, at least in terms of the Volcker Rule.

Mr. ROTHFUS. As you know, the chairman reached out to you at the beginning of the year for a status update on a number of initiatives that are designed to facilitate capital formation and ensure that the U.S. capital markets remain the leader, rather than focusing on politically divisive issues.

For example, the chairman asked for the status of potential SEC efforts to modernize the rules governing transfer agents. This topic, although highly technical, is of interest to me because the rules have not been updated since the 1980's. I also think it is a rare occurrence when you have bipartisan support within the SEC, given that former Commissioner Gallagher and current Commissioner Aguilar—their statement in June of this year.

In February 2015, you stated in your response letter to the chairman that the SEC staff is considering recommendations. I would like to follow up with the chairman's request for a status update as of today?

Ms. WHITE. We are actually quite actively focused on the transfer agent issues. I don't want to get ahead of what we are going to do or give you a specific date, but I think you will see something coming out quite soon. I don't want to say when, but I mean in the next couple of months.

Mr. ROTHFUS. In what form would that be?

Ms. WHITE. I don't want to say that until it comes out, because one of the things that we are having to balance is that because we haven't updated these rules for 40 years, you need some data to inform yourselves in terms of some of the things that you might propose. There may be other things that you can tee up as a direction you think you are going in as part of that.

So that is really what we are trying to balance, to be as pinpointed as we can, but also make sure we get the input we need by whatever form we put this out in, so—

Mr. ROTHFUS. So you haven't made a determination whether it is going to be a concept release or some other release?

Ms. WHITE. We have not, although we are thinking about maybe some combination.

Mr. ROTHFUS. Mr. Gallagher and Commissioner Aguilar said, "A lengthy delay in updating the Commission's transfer agent rules will be bad for the markets, investors, and issuers. A concept release may be warranted to gather additional information and viewpoints on certain topics, but there are critical reforms requiring immediate action that we can propose now." Would you agree with that?

Ms. WHITE. Yes, and not only do I agree with that, but I asked them to do it, in other words, to come back with areas of agreement. So I do agree with that.

Mr. ROTHFUS. Let's see. You have questioned whether SEC disclosure powers are best used to address societal ills, noting in a speech that, "Other mandates, which invoke the Commission's mandatory disclosure powers, seem more directed at exerting societal pressure on companies to change behavior, rather than to disclose financial information that primarily informs investment decisions.

"That is not to say that the goals of such mandates are not laudable, indeed most are. Seeking to improve safety in mines for workers or to end horrible human rights atrocities in the Democratic Republic of the Congo are compelling objectives, which as a citizen, I wholeheartedly share. But as the Chair of the SEC, I must question, as a policy matter, using the Federal securities laws and the SEC's powers of mandatory disclosure to accomplish these goals."

What is the cost to investors when there is an overemphasis on mandatory disclosure requirements that seem to be targeting societal ills, rather than what may be considered "material" by a company?

Ms. WHITE. It is hard to say what the cost is, obviously, and investors can see things differently.

I think I went on in that speech to say, though, that if it is a congressional mandate, even if as described in the prior remarks, I do consider it our obligation to carry that out.

Mr. ROTHFUS. As you know, last April the U.S. Court of Appeals found that the SEC's conflict minerals rule violated the First Amendment because it required companies to shame themselves. Given the political and shaming nature of the pay ratio rule, is it unreasonable to assume that the pay ratio rule will likely also violate the First Amendment?

Ms. WHITE. We certainly study that precise issue and we believe it comports with the First Amendment.

Mr. ROTHFUS. This week, Commissioner Piwowar proclaimed that the SEC's corporate disclosure regime has been hijacked by social activists. Do you agree with Commissioner Piwowar that the

SEC's disclosure rules are meant to serve investors, not special interests?

Ms. WHITE. I certainly agree that our disclosure regime is meant to serve investors. Again, I think that if they are mandated disclosure rules, we have an obligation to carry them out. It is the law.

Mr. ROTHFUS. Can you explain how the SEC's pay ratio rule serves investors over special interests?

Ms. WHITE. I think—and again, it is in the release—what the pay ratio rule does is—and it is a mandated rulemaking obviously—to provide investors another data point in judging a CEO's compensation. That is the finding in the release.

Mr. ROTHFUS. I yield back. Thank you.

Mr. SCHWEIKERT. Thank you, Mr. Rothfus. It looks like it is just us.

Ms. WHITE. Okay.

[laughter]

Mr. SCHWEIKERT. A couple of things, Madam Chair. First off, you have always been very kind to me, and your staff has been terrific, and because of that, I am just going to yield myself as much time as I may consume because I have a lot of questions.

Ms. WHITE. Okay.

Mr. SCHWEIKERT. You already hit the clock on me. Okay, this is—I am going to ask you for almost a narrative answer on this, and pretend no one is watching or listening. Being someone who was both, I think, intellectually and emotionally vested in crowdfunding, in the JOBS Act, in Reg A-plus, but let's use JOBS Act and the crowdfunding portion.

Almost 4 years beyond when the rules should have been done, in something that from the IQ you have around you and yourself, should not have been very complicated. I beg of you, could you walk me through—

Ms. WHITE. Sure.

Mr. SCHWEIKERT. —what happened.

Ms. WHITE. I don't think it was 4 years; I think it was 3 years. Not that that is the answer here—

Mr. SCHWEIKERT. Okay. It is 3-plus. I will give you—well, let's call it 3.

Ms. WHITE. Okay.

Mr. SCHWEIKERT. Look, your staff and others were very kind to let us see some of the letters that were coming from certain union front groups and other groups that disparage crowdfunding. But help me understand, because as this hearing is supposed to be about resources, was this a resource issue, was this a political issue, was it an intellectual capital issue? Why so long?

Ms. WHITE. I have already described how our need for resources is really across-the-board, but this is one where—and I believe I testified to this in March when I was here—we knew this rulemaking was going to be very complicated going into it because the statute is quite prescriptive in some areas, funding portals which are enormously important to investor protection is a complicated piece of that as well.

And then, we did our proposal. I really tried to light a fire under the proposal. We got it out pretty quickly after I got here, I think.

And then the comments came in, and we were trying—and again, we have to work within the statute when it is prescriptive—

Mr. SCHWEIKERT. But—

Ms. WHITE. —but we try to make it—

Mr. SCHWEIKERT. —but also the statute actually had some deadlines too.

Ms. WHITE. No, no, no. I am not—I am just saying we do need to observe those, obviously. Some places give us discretion, some places don't. And the goal is to make it workable and to safeguard investors in the new marketplace. And that proved to be very, very difficult.

Mr. SCHWEIKERT. And what I was asking in my question design—and maybe I need to do this in writing because some of this is uncomfortable—is the power of certain activist groups to delay something at the same time both the right and the left here get behind these microphones and talk about the desperate need for economic growth and the new economy and the future that brings us, and then some of the things that we tell our constituents we are doing for them to grow the economy take 3 years to get a rule set done.

Ms. WHITE. But again, I will give you my own perspective. We are talking in the context of crowdfunding. This was done purely on the merits to get it workable, to get it to protect investors. There is no politics, no activism, no anything.

Mr. SCHWEIKERT. In that time, what, 2 dozen States actually did their own and produced their own rule sets and are up and running.

Ms. WHITE. Yes, but they also did not have the same statutory framework we had to work with, and it is not a Federal rule. And I mentioned it earlier, one of the really important, I think, exciting things we did the same day we did crowdfunding are these amendments to Rules 147 and 504, because that is really quite solicitous of those State crowdfunding statutes too. Obviously, it is a proposal at this point, but I think that is a good thing.

Mr. SCHWEIKERT. If done robustly, there is actually an interconnectivity there that actually could be very helpful for the economy. And this is one of those—just because as I was walking out to grab a meeting, I thought I heard something in a previous question, I think with Representative Luetkemeyer. And it sounded like the regulatory or additional regulatory scrutiny when an investment organization will pledge their holdings up for shorts or a loan on their book. Did I pick up something there—

Ms. WHITE. I don't think so.

Mr. SCHWEIKERT. All right. Last one, it is also important to us. We accept that your Commission, the Board right now is short one Republican. There is a certain nervousness out there that in the waning days of an Administration, the independence of the SEC—this is more of just a request for your greatest prudence as rules are being brought for a vote of yourself and your fellow Commissioners that you are shorthanded and something that would be controversial, have a cascade effect policywise, be dealt in that light that there is a voice missing.

Ms. WHITE. Again, I think literally and otherwise, I am extraordinarily independent. We try to do these rulemakings on the merits. Obviously, I think we have had an allusion to the 3–2 votes that we have had. And that is sort of part of the landscape, I think at this point in time. We need to move forward with the agenda, but I certainly will be sensitive to all things.

Mr. SCHWEIKERT. And because I have no one else waiting, I am going to give myself a couple of extra moments here. For the SEC and your team, how much interest and focus is there, shall we say, on the new economy? As we see Silicon Valley is spending lots and lots of resources trying to find ways to provide financial service-type products, lending products, crowdfunding platforms or other types of platforms, do you have someone on your team who actually now is specializing in trying to say, this is our future, this is coming at us, here is new technology—

Ms. WHITE. Yes, is the answer to that. One of the things that we have been doing for the last several years is to make sure that we have, I am going to call it the market expertise, but really, the points of view that would encompass the new products, the new innovations on—

Mr. SCHWEIKERT. Are there some things—because this is one of the things in our lives that actually may be bipartisan—we can do as policymakers to provide you with tools or statutory mechanics to allow you to embrace and run with those ideas that are good and do it as fast as possible so we are not slowing down what many of us believe is our future of our economic growth, and that is the new economy?

Ms. WHITE. What really helps us is that outside expertise genius, that we make sure that we have in-house when we can. And we do try to do that.

Mr. SCHWEIKERT. Okay. Chair White, thank you so kindly for your patience and the time you gave us today.

Ms. WHITE. Thank you very much. Thank you.

Mr. SCHWEIKERT. I would like to thank our witness.

The Chair notes that some Members may have additional questions for this witness, which they may wish to submit in writing. Without objection, the hearing record will remain open for 5 legislative days for Members to submit written questions to this witness and to place her responses in the record. Also, without objection, Members will have 5 legislative days to submit extraneous materials to the Chair for inclusion in the record.

And with that, this hearing is adjourned.

[Whereupon, at 1:09 p.m., the hearing was adjourned.]

A P P E N D I X

November 18, 2015

Testimony on "Examining the SEC's Agenda, Operations, and FY 2017 Budget Request"
by
Chair Mary Jo White
U.S. Securities and Exchange Commission

Before the
Committee on Financial Services
United States House of Representatives
November 18, 2015

Chairman Hensarling, Ranking Member Waters, and Members of the Committee:

Thank you for inviting me to testify regarding the recent activities and current initiatives of the U.S. Securities and Exchange Commission (SEC).[1] As you know, the SEC has a three-part mission: to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation. Since I last testified before this Committee eight months ago, the SEC has advanced significant rulemakings, continued to bring strong enforcement actions against wrongdoers, and made significant progress on our initiatives involving the asset management industry, equity market structure, and disclosure effectiveness.

As described in more detail below, the Commission has adopted or proposed 17 substantive rulemakings in the past eight months, including rules required by the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) and the Jumpstart Our Business Startups Act (JOBS Act). These efforts have included final rules addressing over-the-counter derivatives; new means for small businesses to access capital (including rules to update Regulation A and permit securities-based crowdfunding offerings); executive compensation disclosures; and the removal of references to credit ratings from our rules. In addition to implementing congressionally mandated rules, we have also advanced other important programs, including rules to enhance oversight of high-frequency traders and our supervision of investment advisers and mutual funds.

Our enforcement program also continued to deliver very strong results, with the Commission bringing 807 enforcement actions and obtaining monetary remedies of approximately $4.2 billion in Fiscal Year 2015 (FY 2015). These results included high-quality, "first-ever" cases in a number of important areas, including protections for whistleblower communications; violations by financial institutions under the Foreign Corrupt Practices Act; misconduct by underwriters in the primary market for municipal securities; and the fee practices of private equity advisers. In addition, the Commission brought cutting edge market structure enforcement cases, including an action against a dark pool operator for running a secret trading desk and an action against a high frequency trading firm for violating the market access rule and Regulation NMS. The Commission also continued to seek admissions, including the first-ever admissions settlement with an auditing firm, and to pursue complex cases with criminal

[1] The views expressed in this testimony are those of the Chair of the Securities and Exchange Commission and do not necessarily represent the views of the full Commission, or any Commissioner.

authorities, including a recent action charging dozens of defendants with a global scheme to profit from hacked non-public information about corporate earnings announcements.

Going forward, we plan to continue to focus on completing our mandatory rulemakings while pursuing other initiatives that are critical to our mission, including those relating to asset manager oversight, equity market structure, and our disclosure effectiveness review. We will also continue to strengthen our enforcement and examination programs, striving for high-impact efforts that protect investors and preserve market integrity. The agency's Fiscal Year 2017 budget request to the Office of Management and Budget reflects these priorities, focusing on the execution of our core programs and operations by seeking to hire individuals with the skill sets necessary to enhance the agency's oversight of increasingly complex securities markets; striving to build the significant new oversight programs assigned to the SEC in recent years; and continuing to enhance our technology, including our ability to analyze and assess large volumes of data.

I deeply appreciate the serious responsibility we have to be prudent stewards of the funds we are appropriated, and we strive to demonstrate how seriously we take that responsibility by the work we do. We continue to place a high priority on allocating our resources efficiently and effectively, and we were very pleased that the Commission recently received an unmodified audit report, the agency's best-ever audit opinion from the Government Accountability Office, with no material weaknesses or significant deficiencies identified in FY 2015. With Congress' continued assistance, we plan to build on these improvements and continue to enhance the execution of our mission.

Implementing Remaining Congressional Mandates and Other Significant Rulemakings

Since I last testified, the SEC has continued to make substantial progress implementing the rulemakings mandated by the Dodd-Frank and JOBS Acts, completing significant rulemaking in key areas under the Dodd-Frank Act and finishing all major rulemakings under the JOBS Act. Specifically, since the hearing on March 24, 2015, the Commission has:

- Adopted final rules to update and expand Regulation A (commonly referred to as Regulation A+), an exemption from registration for small offerings of securities, to facilitate smaller companies' access to capital;

- Adopted new rules under Title VII of the Dodd-Frank Act to provide a comprehensive, efficient process for security-based swap dealers and major security-based swap participants to register with the SEC and proposed new procedures addressing statutorily disqualified associated persons;

- Adopted new rules to permit securities-based crowdfunding offerings by issuers and the operation of funding portals to intermediate such offerings;

- Adopted amendments to remove credit rating references in the principal rule that governs money market funds and the form that money market funds use to report information to the Commission each month about their portfolio holdings;

- Adopted a rule that requires public companies to disclose the ratio of the compensation of their chief executive officer to the median compensation of its employees;

- Proposed rules governing the application of certain requirements to security-based swap transactions connected with a non-U.S. person's dealing activity in the United States;

- Proposed rules to require companies to disclose the relationship between executive compensation and the financial performance of a company;

- Proposed rules directing national securities exchanges and associations to establish listing standards requiring companies to adopt policies that require recovery of incentive-based compensation erroneously awarded to executive officers; and

- Proposed amendments related to regulatory access to security-based swap data held by security-based swap data repositories.

The Commission has also acted in the last eight months to advance other important rules central to investor protection, market integrity, and capital formation, a number of which are connected with the larger initiatives described in detail below. The Commission:

- Proposed rules to require that broker-dealers trading in off-exchange venues become members of a national securities association to enhance regulatory oversight of active proprietary trading firms, such as high-frequency traders;

- Proposed two sets of rules to modernize the reporting and disclosure of information by investment companies and investment advisers to enhance the quality of information available to investors and allow the Commission to more effectively collect and use data provided by investment companies and investment advisers;

- Proposed rules designed to promote effective liquidity risk management for open-end funds (except money market funds) and permit the use of swing pricing for open-end funds (except money market funds and exchange-traded funds (ETFs));

- Proposed amendments to Securities Act Rule 147 to modernize the rule for intrastate offerings, including through intrastate crowdfunding provisions, and to Rule 504 to increase the aggregate limit on offers and sales and to provide additional investor protections;

- Proposed two sets of amendments to the SEC rules governing its administrative proceedings that, if adopted, would among other things adjust the timing of administrative proceedings and permit parties to take depositions of witnesses as part of discovery;

- Issued a request for comment on the effectiveness of financial disclosures about entities other than the registrant under Regulation S-X; and

- Issued a concept release about possible revisions to audit committee disclosures.

Vigorous Enforcement of the Securities Laws

The SEC's vigorous enforcement program is at the heart of its efforts to protect investors and instill confidence in the integrity of the markets. The Division of Enforcement (Enforcement) advances these efforts by investigating and bringing civil charges against violators of the federal securities laws. Successful enforcement actions impose meaningful sanctions on securities law violators, result in penalties and disgorgement of ill-gotten gains that can be returned to harmed investors, and deter further wrongdoing.

Enforcement continued to deliver very strong results on behalf of investors in FY 2015. The SEC filed a record 807 enforcement actions covering a wide range of misconduct, and obtained orders totaling $4.19 billion in disgorgement and penalties. Of the 807 enforcement actions filed in Fiscal Year 2015, a record 507 were independent actions for violations of the federal securities laws, and 300 were either actions against issuers who were delinquent in making required filings with the SEC or administrative proceedings seeking bars against individuals based on criminal convictions, civil injunctions, or other orders.

More important than the numbers, these actions addressed meaningful issues for investors and markets, spanned the securities industry, and included numerous "first-of-their-kind" actions. Significantly, approximately two-thirds of our substantive actions in FY 2015 also included charges against individuals. A few other important features of our enforcement program drawn from the last eight months also bear highlighting.

Leveraging Data Tools and Analysis

Enforcement's leveraging of data and quantitative analytics contributed significantly to the year's strong results. Specifically, Enforcement has focused on ways to harness in-house expertise and data infrastructure to analyze massive data sources and identify conduct that potentially violates the federal securities laws. For example, Enforcement is partnering with our Division of Economic and Risk Analysis to develop a tool to enable staff to detect anomalous financial results disclosed in public company filing data. Enforcement staff is also implementing new analytical tools to detect suspicious trading patterns to assist with insider trading and microcap fraud investigations. These tools can streamline investigations significantly and, in some cases, identify misconduct that previously might not have been detected. These efforts have facilitated a number of cases filed during the past six months.

Executing the Admissions Policy

The Commission continues to aggressively seek admissions in cases where heightened accountability and acceptance of responsibility by a defendant is particularly important and in the public interest. These types of cases include those involving particularly egregious conduct; where large numbers of investors were harmed; where the markets or investors were placed at significant risk; where the conduct undermines or obstructs our investigative process; where an admission can send an important message to the markets; or where the wrongdoer presents a particular future threat to investors or the markets. Since adopting the admissions protocol in 2013, the SEC has obtained admissions in more than thirty cases (and from a total of 47 entities and individuals), including a number involving a major financial institution and a national auditing firm and requiring charged individuals to admit liability in a world-wide pyramid scheme targeting the Asian-American community. As we indicated when we adopted the admissions protocol, the majority of cases continue to be resolved on a "neither admit nor deny" basis.[2] We continue, however, to increase the use of our evolving, "first-of-its-kind" policy to require admissions or other acknowledgements of wrongdoing where appropriate, and will be prepared to litigate those cases if necessary.

Focusing on Key Areas of Misconduct

The Commission also continues to focus resources on key areas of misconduct. One critical area is financial reporting and issuer disclosure. Comprehensive, accurate, and reliable financial reporting is the bedrock upon which our markets are based, and our Enforcement Division is focused on pursuing violations in this area. The SEC brought a series of significant financial reporting cases in FY 2015, including four important actions in September, each of which also involved charges against senior executives.

Another key area is investment management, where the SEC has continued to bring actions addressing a wide range of issues, such as performance advertising, undisclosed conflicts of interest, compliance issues, and private equity fees and expenses. These include "first-of-their-kind" actions for failures to report material compliance matters to fund boards and the improper allocation of expenses by private equity advisers.

Enhancing the Whistleblower Program

The SEC's Whistleblower program continues to have a transformative impact on our enforcement program. The SEC's Office of the Whistleblower is currently tracking over 700 matters in which a whistleblower's tip has caused a matter under investigation or an investigation to be opened, or which have been forwarded to Enforcement staff for consideration in connection with an existing investigation. In FY 2015, the Commission paid more than $37 million to eight whistleblowers who provided original information that led to successful enforcement actions resulting in an order or monetary sanctions exceeding $1 million, and has awarded more than $50 million since the program's inception. The Commission also brought actions against firms for whistleblower retaliation and improper restrictions of whistleblowing activity in confidentiality agreements.

[2] In many cases, the Commission, like other federal agencies with civil enforcement powers, determines that it is appropriate to continue to settle on a "no admit, no deny" basis. This practice allows the Commission to obtain significant relief, eliminate litigation risk, return money to victims more expeditiously, and conserve enforcement resources for other matters.

Building New Initiatives for Facilitating Capital Formation

On this strong foundation of rulemaking and enforcement, we have continued to advance programs to address issues central to the Commission's mission using all of the tools available to us. These programs have sought to expand capital formation for small businesses, review the effectiveness of our disclosure regime, enhance the oversight of asset managers, enhance our equity and fixed income market structure, and catalyze consideration of a uniform fiduciary duty for investment advisers and broker-dealers.

With the adoption of the rules for both Regulation A+ and crowdfunding, the Commission is moving beyond the program set forth by the JOBS Act to develop a number of ongoing initiatives that are designed to facilitate capital formation, particularly for small businesses.

Last month, the Commission issued a rule proposal seeking to modernize Rule 147, a safe harbor to a statutory exemption for intrastate securities offerings, which would establish a new exemption to facilitate capital formation through intrastate offerings. Many market participants and state regulators have raised concerns that the current requirements of Securities Act Section 3(a)(11) and Rule 147 have not kept up with changes in the business environment and technology, which limits the usefulness of the exemption for capital-raising, especially for smaller state and local businesses. The rule proposal would retain the key feature of existing Rule 147 – its intrastate character, which permits companies to raise money from investors within their state without concurrently registering the offers and sales at the federal level. In recognition of the transformative nature of the internet and other technologies, however, the rule would, among other things, eliminate the existing intrastate restriction on offers, but – critically for the state-based nature of the offering and its regulation – would require that sales be made only to residents of the state or territory of the issuer's principal place of business. The proposal would also ease some of the issuer eligibility requirements to make the rule available to a greater number of businesses seeking financing in state, but ensure that such financing can only occur with a set of baseline investor protections and that issuers have a strong and identifiable presence within the state of offering.[3]

In May of this year the Commission also approved a proposal, submitted in response to a Commission order, by the national securities exchanges and the Financial Industry Regulatory Authority (FINRA) for a two-year pilot program that would widen the minimum quoting and trading increments – or tick sizes – for stocks of some smaller companies. The SEC plans to use the pilot program to assess whether wider tick sizes enhance the market quality of these stocks for the benefit of issuers and investors.

In addition, as described in more detail below, the Division of Corporation Finance currently is engaged in a comprehensive review of the disclosure requirements for public companies, including smaller public companies, with the goal of making recommendations on

[3] While the proposed rule could be used for any intrastate offering meeting its conditions, more than 25 states have enacted some form of intrastate crowdfunding, and this provision could facilitate capital raising through those state provisions.

how to update the requirements to facilitate timely, material disclosure by companies and shareholders' more usable access to that information. The staff is also engaged in a comprehensive review of the "accredited investor" definition. That review and the feedback received through that process will inform the SEC's consideration of whether to change the definition of accredited investor, including whether net worth and annual income should be used as tests for determining whether a natural person is an accredited investor, and at what levels. As part of that review, the staff also plans to independently evaluate alternative criteria for the definition suggested by the public or other interested parties, giving careful consideration to both the need to facilitate capital formation and the need to protect investors.

The Office of Small Business Policy within the Division of Corporation Finance also continues to provide extensive guidance to small businesses seeking to raise capital or comply with our reporting requirements. Each year the office responds to over 1,000 requests for interpretive advice, provides guidance through speaking engagements and meets frequently with interested parties about pending rulemakings that could impact small businesses.

Disclosure Effectiveness Review

As discussed above, as follow-up to the Regulation S-K[4] study required by the Dodd-Frank Act, I directed the staff to develop specific recommendations for updating disclosure requirements. The goal is to comprehensively review the existing disclosure requirements and make recommendations to the Commission on how to update the requirements to facilitate timely, material disclosure by companies and shareholders' more usable access to that information. The staff is currently considering ways to improve the disclosure requirements, including those in Regulation S-K and Regulation S-X,[5] for the benefit of investors and companies.

The staff is reviewing the disclosure requirements in phases. In the first phase of the review, the staff is focusing on the business and financial disclosures required by periodic and current reports, Forms 10-K, 10-Q and 8-K, and updates to certain Industry Guides. The staff also will consider whether disclosure requirements should be scaled for certain categories of issuers, such as smaller reporting companies or emerging growth companies, and, if so, how. In August, as noted above, the Commission issued a Request for Comment for certain disclosure requirements in Regulation S-X.

The staff is also considering how companies file their disclosures and is exploring alternatives that could enhance the way that investors access the disclosures. In the near term,

[4] Regulation S-K is the central repository for the Commission's non-financial disclosure requirements. It is intended to foster uniform and integrated disclosure for registration statements under the Securities Act of 1933, registration statements under the Securities Exchange Act of 1934 (Exchange Act), and periodic and current reports filed under the Exchange Act.

[5] Regulation S-X contains disclosure requirements that dictate the form and content of financial statements to be included in filings with the Commission. It addresses both registrant financial statements and financial statements of certain entities other than the registrant. It also requires that domestic issuer financial statements filed with the Commission be prepared in accordance with generally accepted accounting principles.

we are working on changes to sec.gov that would make EDGAR filings more accessible to investors and easier for them to navigate. In a later phase of the review, the staff will review and consider recommendations regarding the governance and compensation disclosures required in proxy statements.

To date, we have heard from a number of interested parties about this review, receiving over 50 separate comment letters. We expect this number will increase as the Commission issues additional concept and proposing releases.

Enhancing Risk Monitoring and Regulatory Safeguards for the Asset Management Industry

As our rulemaking efforts since March illustrate, the Commission and its staff have made significant progress in executing a program to enhance risk monitoring and regulatory safeguards for the asset management industry.

On May 20, 2015, the Commission proposed new rules and forms as well as amendments to its rules and forms to modernize the reporting and disclosure of information by registered investment companies. The proposed rules, if adopted, would include the following enhancements:

- *Portfolio Reporting.* A new monthly portfolio reporting form, Form N-PORT, would require registered funds other than money market funds to provide portfolio-wide and position-level holdings data to the Commission on a monthly basis.

- *Census Reporting.* Registered funds would be required to annually report certain census-type information to the Commission on Form N-CEN, and the form currently used to report fund census information (Form N-SAR) would be rescinded. Proposed Form N-CEN would streamline and update information reported to the Commission to reflect current information needs, such as requiring more information on ETFs and securities lending.

- *Structured Data.* Funds would report portfolio and census information in a structured data format, which would improve the ability of the Commission and the public both to aggregate and analyze information across all funds and to link the reported information with information from other sources.

- *Enhanced Disclosure and Website Communications.* Funds would be required to provide enhanced and standardized financial statement disclosures, and could provide shareholder reports by making them accessible on their website, while providing shareholders the option of continuing to receive paper copies.

Also on May 20, 2015, the Commission proposed amendments to Form ADV, the primary investment adviser reporting and disclosure form, that would: (1) provide additional information regarding advisers, including information about their separately managed account business; and (2) address issues that staff has identified since the Commission made significant changes to Form ADV in 2011.[6] In addition, the proposed amendments would, if adopted, require advisers to maintain records of the calculation of performance information that is distributed to any person.

On September 22, 2015, the Commission proposed a new rule that would require open-end funds to adopt and implement liquidity management programs. If the proposed rules are adopted, they would effect the following enhancements, among others:

- *Liquidity Risk Management Programs.* Mutual funds and other open-end management investment companies, including ETFs, would be required to have a liquidity risk management program. The proposed rule would exclude money market funds from the requirements because they are already subject to liquidity requirements tailored to their particular structure and operations.

- *Swing Pricing.* Mutual funds (except money market funds or ETFs) would be permitted to use "swing pricing."[7]

- *Enhanced Disclosures.* Mutual funds and other open-end funds would be required to provide enhanced disclosure regarding fund liquidity and redemption practices, the methods used by funds to meet redemptions, and, if used, swing pricing. Funds would also be required to disclose information regarding committed lines of credit, interfund borrowing and lending, and swing pricing.

The comment period for the proposed rules on data modernization and liquidity management will be open through January 13, 2016. The Commission has already received substantial public comment, and all comments received will be analyzed in connection with the staff's development of recommendations to the Commission on final rules.

At my direction, the SEC staff is working on additional initiatives aimed at helping to ensure the Commission's regulatory program is fully addressing the increasingly complex portfolio composition and operations of the asset management industry. These initiatives include:

- *Use of Derivatives by Investment Companies.* SEC staff is working on recommendations to the Commission to propose new requirements related to the use of derivatives by registered funds, including measures to appropriately limit the leverage these instruments may create and enhance risk management programs for such activities.

[6] For example, the proposals would, if adopted, require aggregate information related to assets held and use of borrowings and derivatives in separately managed accounts and provide additional information about an adviser's advisory business, including branch office operations and the use of social media.

[7] Swing pricing is the process of reflecting in a fund's net asset value the costs associated with the trading activity of the fund occasioned by shareholders' redemptions and purchases in order to reflect those costs in the prices paid and received by purchasing and redeeming shareholders.

- *Transition Plans for Investment Advisers.* Staff is also developing recommendations for the Commission to propose requiring investment advisers registered with the Commission to create and maintain transition plans to prepare for a major disruption in their business.

- *Stress Testing for Large Investment Advisers and Large Investment Companies.* Staff is also considering recommending that the Commission propose new requirements for stress testing by large investment advisers and large investment companies. Such rules would implement in part requirements under section 165(i) of the Dodd Frank Act.

- *Third-Party Compliance Reviews.* At my direction, staff is also preparing a recommendation to the Commission for proposed rules requiring third-party compliance reviews for registered investment advisers. The reviews would not replace examinations conducted by our Office of Compliance Inspections and Examinations, but would be designed to improve overall compliance by registered investment advisers.

Enhancing Our Equity and Fixed Income Market Structure

Since I last testified, we have proceeded with our ongoing assessment of U.S. equity market structure to ensure that our markets remain the deepest and fairest in the world and optimally serve investors and companies of all sizes seeking to raise capital.

As noted above, the Commission approved the initiation of a pilot on different tick sizes, and the SEC staff continues to work with the exchanges and other market participants to implement the pilot. The data generated by this initiative will deepen our understanding of the impact of tick sizes on market quality and help us consider new policy initiatives that can improve trading in the securities of smaller-cap issuers. In addition, the Commission proposed important amendments to Rule 15b9-1 to require broker-dealers that engage in off-exchange proprietary trading to become members of a national securities association, which would extend self-regulatory oversight to a significant portion of off-exchange trading not currently so regulated.

In February, the Commission established the Equity Market Structure Advisory Committee to provide a formal mechanism through which the Commission can receive advice and recommendations on equity market structure issues. The first meeting, held on May 13, 2015, focused on Rule 611 of Regulation NMS, known as the "Order Protection Rule" or "Trade-Through Rule." The second meeting, held on October 27, 2015, focused on two important market structure topics – the impact of access fees and rebates widely used by stock exchanges and the regulatory structure of trading venues. Following the second meeting, the Committee established subcommittees to look more closely at specific issues identified by the SEC staff and Committee members before presenting them to the full Committee for discussion and deliberation. The staff and the Committee will continue to use a variety of tools to ensure both the transparency of the Committee's consideration of issues and input from the full range of investors and other interested market participants, as well as from other advisory committees and organizations with remits that overlap with the Committee's.

In addition, the Commission will shortly take up another important proposal for reform in our equity markets, amending Regulation Alternative Trading System (ATS) to require enhanced transparency with respect to ATSs that trade national market system stocks. In the years since Regulation ATS was first adopted in 1998, our equity markets have undergone significant change. Advancements in technology have fueled the growth in the number of trading centers and trading activity in NMS stocks is less concentrated. ATSs are an important component of our current market structure, as they compete directly with national securities exchanges and account for approximately 15% of the dollar volume in NMS stocks. The proposal that the Commission will soon consider would, if adopted, update our regulation of these trading venues by requiring enhanced public disclosures.

Beyond Commission rulemaking, in response to requests I have previously made, all of the exchanges have conducted and completed in-depth analyses of order types and have filed proposed rule changes to reflect their findings. All of the exchanges have also now submitted rule filings disclosing how they use securities information processor (SIP) feeds and direct feeds. These filings provide significantly improved transparency for investors and the public on how the exchanges operate. Also at my request, the SIPs have implemented a time stamp in their data feeds, to facilitate greater transparency on the issue of data latency.

The staff also continues to progress on recommendations to the Commission to address, among other things:

- The registration status of certain active proprietary traders and improvements to firms' risk management of trading algorithms;
- Enhanced disclosure requirements concerning a broker's order routing practices;
- An anti-disruptive trading rule that would address the use of aggressive, destabilizing trading strategies in vulnerable market conditions; and
- The development and implementation of a consolidated audit trail.

With respect to our fixed income markets, I have directed SEC staff to undertake an initiative designed to enhance the public availability of pre-trade pricing information in the fixed income markets. This initiative builds on a recommendation in the Commission's July 2012 Report on the Municipal Securities Market, and would potentially require the public dissemination of the best prices displayed by market participants on electronic systems, such as ATSs and other electronic dealer networks, in the corporate and municipal bond markets. This potentially transformative change would broaden access to pricing information that today is available only to select parties, and could facilitate enhanced execution, improve market efficiency, and promote price competition. I am mindful, however, of the need to strike the right balance of compelling the disclosure of meaningful pre-trade pricing information without discouraging market participants from producing such information. Accordingly, to help inform our initiative on pre-trade price transparency, we have been actively engaged in discussions with market participants, FINRA, and the Municipal Securities Rulemaking Board

(MSRB). Before we take any actions, I also anticipate careful staff analysis of the pricing data already available to assess how best to achieve our regulatory objectives.

On September 24, 2015, the MSRB published a request for comment on a new proposal that would require confirmation disclosure of mark-ups for certain principal transactions with retail customers when the dealer makes a corresponding trade within two hours of the customer's trade. The MSRB also requested comment on proposed modifications to a November 2014 proposal that would require confirmation disclosure of same-day pricing information for specified principal transactions with retail customers. On October 12, 2015, FINRA published a request for comment on a modified proposal that would require confirmation disclosure of same-day pricing information for specified principal transactions with retail customers.

The comment periods for the FINRA and MSRB requests for comment end on December 11, 2015. Although these proposals differ to a degree, FINRA and the MSRB have represented that they intend to coordinate on their approach to potential rulemaking in this area. Staff in the SEC's Office of Municipal Securities and Division of Trading and Markets have been closely monitoring these proposed changes and look forward to hearing from commenters in light of the goal we share with the MSRB and FINRA of providing meaningful dealer compensation disclosure to retail investors.

Personalized Investment Advice Standard of Conduct

Section 913 of the Dodd Frank Act granted the Commission authority under the Exchange Act and Advisers Act to adopt rules establishing a uniform fiduciary standard of conduct for broker-dealers and investment advisers when providing personalized investment advice about securities to retail customers. In March 2013, the Commission issued a public request for information to obtain further data and other information to assist it in determining whether or not to use the authority provided under section 913 of the Dodd Frank Act.

As I indicated previously, my evaluation of the differences in the standards that apply to advice under the federal securities laws has led me to conclude that broker-dealers and investment advisers should be subject to a uniform fiduciary standard of conduct when providing personalized investment advice about securities to retail investors. I recognize that this is a complex issue, and that there are significant challenges that will need to be addressed in proposing a uniform fiduciary standard, including how to define the standard, how it would affect current business practices, and the nature of the potential effects on investors, particularly retail investors.

SEC staff is developing rulemaking recommendations for the Commission's consideration. As part of its analysis, the staff is giving serious consideration to, among other things, the recommendations of an SEC staff's 2011 study under Section 913 of the Dodd-Frank Act, the views of investors and other interested market participants, potential economic and market impacts, and the information we received in response to the Commission's request for data. Ultimately, of course, the Commission as a whole will decide whether to proceed with a rulemaking to implement a uniform fiduciary duty and, if so, its parameters. I will discuss all aspects of this issue with my fellow Commissioners as we proceed.

Conclusion

The Commission's extensive work to protect investors, preserve market integrity, and promote capital formation is not limited to the above initiatives. But I have tried by example to convey the breadth and importance of the Commission's ongoing efforts and provide a sense of our progress in the last few months.

Thank you for your support of the agency's mission and for inviting me to be here today. Your continued support will allow us to better protect investors and facilitate capital formation, more effectively oversee the markets and entities we regulate, and build upon the significant progress we have made.

I am happy to answer any questions that you may have.

Committee on Financial Services
Examining the SEC's Agenda, Operations, and FY 2017 Budget Request
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Representative Sean Duffy (WI-7)
Questions for the Record
"Examining the SEC's Agenda, Operations and Budget Request for FY 2017"
November 18, 2015

1. **Recently we have seen a bipartisan and public call from SEC Commissioners Aguilar, Piwowar, and former Commissioner Gallagher for the agency to finish its derivatives related rulemakings. While there are many parts of the Dodd-Frank Act I find concerning, the fact is that the persisting regulatory uncertainty is preventing the derivatives markets from adapting, stifling innovation, and killing any chance of new competition. Will you make these derivatives rulemakings a priority and commit to a timeline for completion, rather than continuing to focus the agency's resources and attention on the more political rulemakings as you have to date?**

Response: Continued implementation of Title VII is a major priority for me, the staff, and the entire Commission. While standing up an entirely new regime for this global derivatives market, the Commission has worked to prevent costly disruptions that could result if all new our rules were to go into effect simultaneously, or haphazardly.

We have continued to make significant progress this past year. We finished the rules necessary to deliver transparency to the market through the reporting of derivatives transactions to regulators and the public through registered security-based swap trade repositories, or SDRs. We also adopted rules to provide a comprehensive, efficient process for security-based swap dealers and major security-based swap participants to register with the SEC. These are rules that go to the core of derivatives reform by establishing a strong foundation for transparency and efficiency in the market.

Having adopted a process for registration, we have begun finalizing the rules governing dealers and major participants. We finalized a comprehensive set of business conduct rules and provisions for verifying transactions, and we are now focused on adopting rules for capital, margin, segregation, and recordkeeping. Our goal is to complete these rules this year. Once that is done, the Commission will have implemented the two most critical pieces of the regulatory regime designed to achieve Title VII's objectives for security-based swaps—trade reporting and dealer regulation. The Commission will then turn to the final stages of implementation, addressing mandatory clearing and trade execution, including the registration and regulation of security-based swap execution facilities.

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2. **As the Commission proceeds with its final derivatives rulemakings, it should be mindful of the increased complexity and costs that market participants will suffer if the rules are not harmonized with corresponding rules in related markets, particularly with respect to the CFTC. Will you commit to ensuring the SEC's rules are harmonized to the maximum extent practical to avoid unnecessary burdens and costs on market participants?**

Response: The Commission regularly consults and coordinates with the CFTC on our respective approaches to the application of Title VII. We recognize the importance of consistency where possible and appropriate. There are times, however, when the Dodd-Frank Act's application to security-based swaps may be different from its application to the swaps that are regulated by the CFTC, because the relevant products, entities, and markets themselves are different, and there are practical differences between how swaps and security-based swaps are traded. In addition, the Title VII provisions applicable to the SEC and CFTC differ in certain areas. Notwithstanding these differences, the SEC continues to strive for consistency, where possible and appropriate, and where not possible or appropriate, toward a regulatory framework that is compatible with the CFTC's framework and, importantly, that is workable for market participants.

3. **IEX, a dark pool, has filed an application with the Commission to become a regulated exchange. One of the main benefits of becoming a regulated exchange is that IEX's quotes would be deemed "protected", and this "protected" status is a boon for trading volumes and revenue. However, while SEC rules state that quotes must be "immediately and automatically" accessible in order to be "protected", IEX is proposing to intentionally delay customer orders before they are executed. How could the Commission ever deem an order subject to an intentional delay before it can be executed to be considered "immediately and automatically" accessible?**

Response: On June 17, 2016, the Commission approved Investors' Exchange LLC's (IEX) application to register as a national securities exchange. On the same day, following notice and a period for comment, the Commission issued an updated interpretation that will require trading centers to honor automated securities prices that are subject to a small delay or "speed" bump when being accessed. The Commission's updated interpretation determined that a small delay should not prevent investors from accessing stock prices in a fair and efficient manner consistent with the goals of Regulation NMS, which provides for the "protected" status you reference. In doing so, the Commission interprets the term "immediate" under Rule 600(b)(3) of Regulation NMS as precluding any coding of automated systems or other type of intentional action that would delay access to a security price beyond a *de minimis* amount of time.

IEX began operating as an exchange as of September 2, 2016, and began fully trading with a protected quote on September 15, 2016. SEC staff is closely monitoring the market impacts. The Commission has also directed the staff to conduct a study regarding the effects of intentional access delays on market quality, including price discovery and report back to the Commission with the results of any recommendations.

4. **I am concerned that several ratings agencies are not consistently applying their ratings methodologies to sovereign debt. Specifically, Peru's ratings have not been affected by its long-standing and current selective default on its agrarian reform bonds that were issued as compensation to Peruvian landholders, but other countries' ratings have been affected by their history of default. What steps is the SEC taking to ensure that the ratings agencies are consistently applying their ratings methodologies to all countries including Peru?**

Response: Section 15E(c)(3)(A) of the Exchange Act requires a nationally recognized statistical rating organization ("NRSRO") to establish, maintain, enforce, and document an effective internal control structure governing the implementation of and adherence to policies, procedures, and methodologies for determining credit ratings. Exchange Act Rule 17g-2(a)(6) requires an NRSRO to make and retain a record documenting its established procedures and methodologies used to determine credit ratings. A general description of the procedures and methodologies the NRSRO uses to determine credit ratings must be included in Exhibit 2 to Form NRSRO. Note, however, that Section 15E(c)(2) of the Exchange Act specifically prohibits the SEC from regulating the substance of credit ratings or the procedures and methodologies by which an NRSRO determines credit ratings.

The Dodd-Frank Act requires that the SEC's Office of Credit Ratings conduct an examination of each NRSRO at least annually. The NRSRO examinations cover eight review areas specified in the Dodd-Frank Act and the SEC staff conducts risk assessments to identify different risks for different NRSROs. One of the mandated review areas is whether the NRSRO conducts business in accordance with its policies, procedures, and rating methodologies.

As part of the annual examination of each NRSRO, the staff reviews ratings actions for issuances selected on a test basis to determine whether the NRSRO conducted business in accordance with its policies, procedures, methodologies, criteria, and models in connection with those issuances. The staff also reviews rating files and documentation selected on a test basis of ratings-related activities to evaluate whether each NRSRO adhered to recordkeeping requirements.

To select rating files to review, the staff uses a risk-based sampling process that considers items such as the significance of the rated asset class to the financial markets and the NRSRO's business, the NRSRO's activity in the rated asset class, news reports and developments concerning NRSROs or particular asset classes (including developments in particular countries), tips, complaints and referrals, and information the staff learned during examinations.

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5. **Despite being in default on the agrarian reform bonds for over 20 years and the routine application by several rating agencies of a "selective default" or "restrictive default" to other sovereigns, none of the major ratings agencies have rated Peru as being in default on the agrarian reform bonds or in selective default overall. For those ratings agencies that are being compensated for their ratings of Peru, what actions is the SEC taking to ensure that the ratings agencies have appropriate policies and procedures in place to address and manage conflicts of interests in their ratings of Peru?**

Response: As noted above, the SEC's Office of Credit Ratings conducts an examination of each NRSRO at least annually. The NRSRO examinations cover eight review areas specified in the Dodd-Frank Act, including management of conflicts of interest by the NRSRO.

Section 15E(h)(1) of the Exchange Act requires an NRSRO to establish, maintain, and enforce written policies and procedures reasonably designed to address and manage conflicts of interest. Exchange Act Rule 17g-5(b) identifies certain types of conflicts that an NRSRO must disclose in Exhibit 6 to Form NRSRO ("Exhibit 6"). The NRSRO's written policies and procedures to address and manage these conflicts must be disclosed in Exhibit 7 to Form NRSRO ("Exhibit 7").

Exchange Act Rule 17g-5(c) lists certain conflicts that are strictly prohibited. For example, Rule 17g-5(c)(6) prohibits an NRSRO from issuing a rating where the fee paid for the rating was negotiated, discussed, or arranged by a person within the NRSRO who had responsibility for determining ratings or for developing or approving procedures, methodologies, or models used to determine ratings.

In connection with the annual examinations, the staff assesses each conflict of interest disclosed in Exhibit 6 with the policies and procedures to address and manage those conflicts listed in Exhibit 7 and considers whether the NRSRO may have other types of conflicts of interest that should be disclosed and managed.

6. **I understand the Commission is considering moving forward with a controversial rulemaking related to the use of derivatives by '40 Act investment companies. Given the departure of Commissioner Gallagher, the impending departure of Commissioner Aguilar, and the fact that the President has nominated two Commissioner replacements who should move quickly through the Senate, the timing for this rulemaking seems arbitrary. Shouldn't you wait until you have a full compliment of Commissioners to consider anything this substantive, particularly when it's not required by Dodd-Frank?**

Response: In December 2014, I publicly outlined a regulatory agenda to effect a more comprehensive approach to address the risks associated with the increasingly diverse nature of registered fund holdings and their use of derivatives. I also noted that the Commission staff had focused on these issues for some time and were developing recommendations for rulemaking regarding the use of derivatives by registered funds. A year later, on December 11, 2015, the Commission considered and voted on a recommendation from the staff of the Division of Investment Management to propose an updated and more comprehensive approach to the use of derivatives by mutual funds, exchange-traded funds, closed-end funds, and business development companies. The Commission and its staff are currently collecting and evaluating public comments related to this proposal. While I look forward to the time when Congress has confirmed the full complement of Commissioners, the Commission has an obligation to continue to focus on the many important and pressing matters facing investors and the markets.

7. **Chair White, you and a number of your fellow Commissioners have commented on the need for data to continue to drive decision-making at the SEC. To that end, in May 2015, the Commission proposed rules to enhance the reporting of information on the use of derivatives by 40 Act funds with a stated goal of allowing the SEC to "more effectively collect and use data." Although that May 2015 proposal remains outstanding, it appears that the SEC is planning to propose additional specific requirements for the use of derivatives by funds by the end of this year. How have you gotten comfortable with proposing additional requirements for the use of derivatives by funds when the agency does not yet have robust data about how funds are using derivatives today?**

Response: On December 11, 2015, the Commission voted to propose new Rule 18f-4 under the Investment Company Act of 1940 (the "1940 Act"), which would permit registered investment companies (as well as companies that elect to be treated as "business development companies" under the 1940 Act) to enter into certain types of derivatives transactions and financial commitment transactions, provided that the funds comply with the conditions of the proposed rule. The proposed rule is designed to provide an updated and more comprehensive approach to the regulation of funds' use of derivatives (such as forwards, futures, swaps and written options) and certain other transactions under the 1940 Act.

The proposed rule was developed following more than five years of study by Commission staff that considered the use of derivatives by funds, including whether the existing regulatory framework continues to fulfill the purposes and policies underlying the 1940 Act and is consistent with investor protection. The staff's review included: analysis of funds' derivatives holdings and other sources of information concerning funds' use of derivatives; examining advisers and funds that make use of derivatives; discussing funds' use of derivatives with market participants; and considering other relevant information provided to the Commission concerning funds' use of derivatives, including comment letters submitted in response to a concept release issued by the Commission in 2011.[1] In the course of this review, the staff observed that funds can experience substantial and rapid losses from

[1] Use of Derivatives by Investment Companies under the Investment Company Act of 1940, Investment Company Act Release No. 29776 (Aug. 31, 2011), https://www.sec.gov/rules/concept/2011/ic-29776.pdf.

investments in derivatives and can be forced to sell investments under adverse conditions and take other measures to meet derivatives-related obligations, which can harm investors.

Importantly, in connection with the development of proposed Rule 18f-4, staff from the Division of Economic and Risk Analysis ("DERA") conducted an extensive review of funds' derivatives use and published a white paper describing their findings.[2] DERA's analysis included a random sample of 10 percent of the universe of registered funds,[3] including mutual funds, closed-end funds, and ETFs, as well as business development companies. This analysis showed that, although many funds do not use derivatives, and most funds do not use a substantial amount of derivatives, some funds do use derivatives extensively. In particular, alternative strategy funds, a category that has grown rapidly in recent years, tend to make much greater use of derivatives than traditional funds.

The derivatives rule proposal is part of a broader set of initiatives designed to address the increasingly complex portfolio composition and operations of the asset management industry. Other initiatives, including modernizing investment company reporting and disclosure (including enhanced reporting of information on the use of derivatives by funds), would complement the new regulatory regime we have proposed for registered funds that use derivatives. The proposed rule also requests comment on the data analysis performed by DERA staff and seeks additional data about how funds currently use derivatives in their investment strategies.

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[2] DANIEL DELI, PAUL HANOUNA, CHRISTOF STAHEL, YUE TANG & WILLIAM YOST, DIVISION OF ECONOMIC AND RISK ANALYSIS, SEC, USE OF DERIVATIVES BY REGISTERED INVESTMENT COMPANIES (Dec. 2015), https://www.sec.gov/dera/staff-papers/white-papers/derivatives12-2015.pdf.

[3] The sample was constructed from the universe of funds included in the Morningstar Direct database, which comprised 11,973 registered funds (excluding money market funds) as of June 2015. The analysis was supplemented with data sampled from Form N-SAR filings made by funds with the Commission in 2014, which comprised 12,360 registered funds.

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Questions
Mary Jo White, Chair SEC
"Examining the SEC's Agenda, Operations, and FY 2017 Budget Request"
Submitted by Representative Keith Ellison

Political Disclosure
More than 1.2 million people or groups submitted supportive comments of a rule requiring political spending disclosure from public companies. This rule has been demanded by shareholders who know that political spending can pose a material risk to shareholders.

- **Can we expect the recommendations following the review process to reflect the popularity of this rule?**

Response: While I recognize and deeply respect the very strong and differing views that have been expressed on this issue from a range of stakeholders, including members of Congress, the subject of mandatory disclosure of corporate political spending is not on the SEC's current Regulatory Flexibility Act agenda. The agenda for this fiscal year continues to focus largely on completing the SEC's congressional mandates and also addresses certain additional mission-critical areas, such as targeted enhancements to the structure of the U.S. equity markets, new regulatory safeguards in the asset management industry, and a review of the effectiveness of our disclosure regime. As you know, the Appropriations Act for FY 2016 prohibited the SEC from using any funds to finalize, issue, or implement any rule, regulation, or order regarding the disclosure of political contributions, contributions to tax exempt organizations, or dues paid to trade associations. The current Continuing Resolution continues that prohibition.

- **Should the SEC require a board resolution to support any particular political contribution?**

Response: Imposing a requirement for director approval of corporate spending on any matter is a substantive corporate governance provision within the ambit of state corporate law and not within our jurisdiction.

CEO-Median Worker Pay Ratio

I am pleased to see that the SEC has finalized its CEO-Median Worker pay ratio rule. The gap between CEO and workers' pay has grown substantially: From 20:1 to more than 300:1. One reason CEO pay has grown so much is the use of stock options as compensation. Many argue that paying CEOs in stock options encourages them to prioritize their personal short-term benefit over the long-term needs of workers, investors and the firm.

Many have called to eliminate the CEO performance pay loophole in Section 162(m). Because stock options are considered performance-based under Section 162(m), their deductibility is unlimited.

- **What are your thoughts about restricting the deductibility of stock options?**

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- **Do you support increasing disclosure requirements on executive compensation and stock options?**

Response: Section 162(m) is part of the U.S. tax code, not the federal securities laws. The Commission's focus is on full and fair disclosure upon which investors can make informed investment and voting decisions. The Commission's disclosure rules currently require substantial disclosure about executive compensation, including about stock options awarded to a company's named executive officers. That disclosure includes detailed information on options granted in the most recent year, options that remain outstanding, and options exercised during the most recent year.

Specifically, our rules require the following disclosures about stock options:

- In the Summary Compensation Table, the aggregate grant date fair value of all options granted to each named executive officer during the last completed fiscal year;
- In the Grants of Plan-Based Awards Table, the individual option awards granted to each named executive officer during the last completed fiscal year, showing the estimated future payouts for performance-based options, the number of shares underlying time-based options, plus the exercise price, grant date, and grant date fair value of each option award;
- Narrative disclosure of the terms of each option award, and, in the Compensation Discussion and Analysis, disclosure of the company's material policies relating to the allocation of compensation among different forms, such as options, that the company uses, and the impact of any material tax treatment on particular forms of compensation;
- In the Outstanding Equity Awards at Fiscal-Year End Table, on an award-by-award basis, the number of securities underlying unexercised options, showing those that are exercisable separately from those that are unexercisable, plus the exercise price and expiration date for each outstanding option; and
- In the Option Exercises and Stock Vested Table, the number of shares acquired and aggregate dollar value realized upon each named executive officer's option exercises during the last fiscal year.

The Commission is always focused on learning whether its rules continue to provide investors with the information that they need to make informed voting and investment decisions. And, as you may know, the staff is engaged in a review of the disclosure requirements applicable to U.S. public companies and is considering ways to improve the disclosure system for the benefit of investors and companies. In April 2016, the Commission issued a concept release on the business and financial information required by Regulation S-K. The comment period on the concept release has closed and the staff is reviewing the comments received. The staff is continuing its review of the disclosure requirements of Regulation S-K, and the Commission recently issued a request for comment on the disclosure requirements relating to information about management, certain security holders, corporate governance, and executive compensation.

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Recently, Senator Tammy Baldwin wrote to you expressing her continued concern about one element of this short term thinking -- stock buybacks. She urges the SEC to be more active in enforcing anti-manipulation provisions of securities laws with respect to buybacks.

- **Do you think stock manipulation through stock buybacks is a problem?**
- **What steps are you taking to investigate the risk that share buybacks could be manipulating stock prices?**

Response: As part of our ongoing mission to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation, the Commission continually works to help ensure that the general anti-manipulation provisions of the federal securities laws and Commission rules are being properly and effectively applied and enforced with respect to all securities transactions, including stock buybacks. In enforcing these anti-manipulation provisions, the Commission's staff closely monitors and pursues through enforcement actions attempts by interested parties (including issuers) to artificially affect a security's market price—whether in pump and dump schemes in which an issuer either itself or indirectly through others touts its common stock through false and misleading statements to the marketplace, or when an issuer is involved in trading to create a false or deceptive picture of the demand for its security, either by placing purchase orders at or near the close of the market to inflate the day's closing price, painting the tape by placing multiple small orders at successively higher prices, or engaging in coordinated matched trading through buy and sell orders for substantially the same amounts and prices. This also includes investigating potential misconduct connected to stock buybacks. For example, the Commission's staff conducts investigations and the Commission brings enforcement actions for manipulation in connection with stock buybacks when parties do not comply with Sections 9(a)(2) and 10(b) of the Securities Exchange Act of 1934, and Rule 10b-5 thereunder.[4] The Commission also investigates and has brought enforcement actions for other misconduct in connection with stock buybacks.[5]

[4] *See, e.g., SEC v. Wey, et al.*, Civil Action No. 15-cv-7116, S.D.N.Y., filed Sept. 10, 2015 (alleging defendants engaged in market manipulation in connection with a stock buyback program under Section 10(b) and Rule 10b-5); *see also SEC v. Competitive Technologies, Inc., et al.*, Civil Action No. 3:04-cv-1331, D. Conn., filed Aug. 11, 2004 (charging defendants with market manipulation in connection with a stock buyback program under Section 10(b) and Rule 10b-5). In *Competitive Technologies*, the court denied defendants' motion to dismiss based on Rule 10b-18 noting that "actions for manipulation that are predicated on allegations and evidence other than the timing, price, amount, and manner of purchases are not barred by Rule 10b–18." *SEC v. Competitive Technologies, Inc., et al.*, 2005 WL 1719725, *3 (D. Conn. July 21, 2005).

[5] *See, e.g., SEC v. Hamilton*, Civil Action No. 3:16-cv-000192-AWT, D. Conn., filed Aug. 30, 2016 (charging defendant with insider trading for trading ahead of company announcements of stock buybacks and other nonpublic financial information); *SEC v. Wang, et al.*, Civil Action No. 13-cv-02270-L-WVG, S.D. Cal., filed Sept. 23, 2013 (charging defendants with insider trading for trading ahead of company announcement of a stock buyback program); *SEC v. Stiefel Lab. Inc. et al.*, 1:11-cv-24438, S.D. Fla., filed Dec. 12, 2011 (alleging that defendants defrauded investors and employees buying using artificially low valuations for stock buybacks).

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Investment Adviser Risk Exams
We act like we are a nation with no resources. We hear calls for austerity. Yet, we have the largest economy in the world. We have a robust financial market but, we do not provide adequate resources to ensure its vitality. Over the last decade the number of registered investment advisers has increased by more than 40 percent to 11,000, and the assets under management increased more than two-fold, to almost $55 trillion. However, the resources available to the SEC to examine investment advisors have severely lagged the number and sophistication of these advisors, which led to staff only being able to examine 10 percent of them last year. Pursuant to the study required by Section 914 of the Dodd-Frank Act, SEC staff provided Congress with three options to increase such examinations, including: imposing a user fee; creating one or more SROs to examine advisers; and authorizing FINRA to examine advisers that are dually registered as broker-dealers.
In testimony before the Appropriations Committee, you indicated that you had asked SEC staff to develop a recommendation for using third-party exams to increase adviser compliance with the Adviser Act.

- **What is your timing for SEC staff to make recommendations to the Commission regarding third-party exams?**

Response: The staff from the Division of Investment Management, working in conjunction with the staff from the Office of Compliance Inspections and Examinations, has prepared a recommendation, which I support, for the Commission's consideration that, if proposed and adopted, would establish a program of independent compliance assessments for registered investment advisers by third parties. That recommendation is before the Commission for its consideration. Although numerous contingencies make the timing of action on this recommendation difficult to estimate, it remains one of my priorities.

- **Do you intend to compare the expenses of such a policy with the other recommendations included in the Section 914 report?**

Response: As the Section 914 report indicated, the options recommended in the report would need to be acted on by Congress to address limitations on existing statutory authority. Over the years, bills have been introduced to address the rate of examinations for investment advisers registered with the Commission, but none have become law. The benefits and costs of reasonable alternative approaches are considered by the Commission as part of the rulemaking process. In addition, if the Commission approves a proposal to establish a program of independent compliance assessments for registered investment advisers, it will contain an economic analysis, including an assessment of reasonable alternatives available to the Commission.

- **Of the recommendations in the report as well as use of third-parties, which is your preferred approach to increasing adviser exams? Which approach is the least cost**

to the U.S. economy? If you do not know, will you study which approach is the least cost to the economy?

Response: As noted above, concern regarding the rate of examinations of investment advisers is not a new issue, and neither are attempts to address the issue through a legislative solution. OCIE has made significant enhancements to its examination program, including hiring additional industry experts, strengthening its examiner training program, and increasing its use of advanced quantitative techniques to enable examiners to more quickly and systematically analyze large amounts of data to detect potential misconduct. After exploring various ways to enhance investor protection and to increase its coverage of investment advisers, OCIE is in the process of transitioning certain resources from its broker-dealer examination program to its investment adviser/investment company examination program, with the goal of increasing examination coverage of investment advisers. But significantly more is still needed.

I have made repeated requests for additional appropriations to hire staff to conduct investment adviser examinations as my preference would be to have additional examinations conducted by OCIE. The recommendation staff is developing to establish a program of independent compliance assessments for registered investment advisers is not designed to be in lieu of examinations by OCIE staff, but rather would be designed to improve overall compliance by registered investment advisers through an independent review.

The staff's recommendations contained in the Section 914 report would result in different costs and benefits. Some commenters have provided an estimate of direct costs of particular recommendations,[6] but neither the Commission staff nor any third parties that I am aware of have done a thorough economic analysis of the report's recommendations or other alternatives that Congress might consider. Accordingly, it is very difficult to determine which approach would have the least cost to the U.S. economy. At this time, I am focused on a feasible regulatory response to the concerns I have regarding investment adviser examinations and compliance, and I have instructed the staff to consider options using the existing authority provided to the Commission.

Enforcement

Estimates of the costs of the financial crisis put the damage to our economy at $13 trillion or more. An entire generation saw its wealth gains erased in a few short years. According to the SEC Enforcement Division Director, the SEC has obtained orders for more than $1.7 billion in financial crisis-related cases, but that the "stream of cases stemming from the financial crisis is coming to an end."

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[6] *See e.g.*, BOSTON CONSULTING GROUP, INVESTMENT ADVISER OVERSIGHT: ECONOMIC ANALYSIS OF OPTIONS (Dec. 2011), https://www.cfp.net/docs/public-policy/bcg_investment_adviser_oversight_economic_analysis.pdf; FINRA, FINRA RESPONSES TO BCG COMMENTS ON FINRA COST ESTIMATE, http://www.finra.org/sites/default/files/Corporate/p126543.pdf.

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- **How many actions have the Commission brought against bad actors related to the financial crisis?**
- **What is the total amount of penalties, fines and disgorgement returned to the US Treasury and investors since the financial crisis of 2008?**
- **How many admissions of guilt, not acknowledgements of facts, have you obtained in connection with cases stemming from the financial crisis?**

Response: The Commission's enforcement record in cases coming out of the financial crisis is strong. Our efforts spanned various types of misconduct involving extraordinarily complex instruments and schemes, and we have brought numerous actions against top executives. To date, the Commission has charged 198 entities and individuals with misconduct related to the financial crisis. This includes actions against 89 CEOs, CFOs, and other senior officers. We have obtained orders for $3.76 billion in penalties, disgorgement, and other financial relief.[7] One of our most recent cases was filed on January 13, 2016.[8]

Since the 2008 financial crisis, enforcement actions filed by the SEC have resulted in significant monetary relief to injured investors or remitted to Treasury, as appropriate. For all SEC enforcement actions filed during fiscal years 2009 through 2015 (including financial crisis cases), more than $5.8 billion has been distributed to injured investors or returned to Treasury.[9]

In June 2013, at my urging, the Commission changed its long-standing settlement protocol by requiring admissions of misconduct in certain cases where heightened accountability and acceptance of responsibility by a defendant are appropriate and in the public interest. Most of the Commission's actions arising out of the financial crises were filed before this change was made. However, we obtained admissions in a case arising out of the financial crisis that was filed after June 2013.[10] Consistent with Commission practice, the respondent in that case admitted the underlying facts and acknowledged that its conduct violated the federal securities laws.

Barring bad actors as an enforcement tool

[7] The $1.7 billion figure mentioned by Enforcement Division Director Ceresney in his March 19, 2015 testimony before the House Financial Services Committee, which appears to be the source of the amount cited in the question, refers to the amount ordered in financial crisis cases brought by the Enforcement Division's Complex Financial Instruments specialized unit. *See* Andrew Ceresney, Dir., Div. of Enf't, SEC, Oversight of the SEC's Division of Enforcement, Testimony Before the Committee on Financial Services, Subcommittee on Capital Markets and Government-Sponsored Enterprises, U.S. House of Representatives (Mar. 19, 2015), http://www.sec.gov/news/testimony/031915-test.html. The $3.76 billion figure includes orders obtained in *all* Commission enforcement actions involving misconduct related to the financial crisis.

[8] *See* Press Release 2016-7, SEC, SEC Charges 11 Bank Officers and Directors with Fraud (Jan. 13, 2016), http://www.sec.gov/news/pressrelease/2016-7.html.

[9] This figure excludes amounts collected by entities other than the SEC (courts, receivers, etc.), and includes small amounts in fees and taxes required on distributions to injured investors.

[10] *See* Press Release 2014-172, SEC, Bank of America Admits Disclosure Failures to Settle SEC Charges (Aug. 21, 2014), https://www.sec.gov/News/PressRelease/Detail/PressRelease/1370542719632; Bank of America Corp., Exchange Act Release No. 72888 (Aug. 21, 2014), http://www.sec.gov/litigation/admin/2014/34-72888.pdf.

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Recently, you stated that the bad actor bars are not enforcement tools and serve distinct purposes from the enforcement remedies. SEC Enforcement Director Ceresney has also said that the Division of Enforcement is not involved in making recommendations about waivers of bad actor bars and the bars are not a bargaining chip for enforcement actions. However, in 2010 the Inspector General of the SEC issued a report regarding the 2009 settlement with Bank of America and specifically found that despite objections from the Division of Corporation Finance, Enforcement staff recommended that the Commission accept a Settlement with Bank of America that was contingent upon regulatory waivers.

- **To what extent is Enforcement Division staff currently involved in the granting or denying of waivers?**
- **To what extent do you or your staff consider waivers as a negotiable term when fashioning settlements?**
- **Does the Enforcement Division and the enforcement staff change the complaint language to avoid disqualification necessitating a waiver?**
- **After getting disqualified, how do you enforce the disqualification?**

Response: It is the Enforcement Division's responsibility to investigate and recommend charges against violators of the federal securities laws. In some cases, these charges will trigger disqualifications under the securities laws and the subjects of these disqualifications will request a waiver. Enforcement Division staff is not responsible for evaluating or making a determination on waiver requests. These determinations are made by the Commission or, in some cases, by staff through authority delegated by the Commission.

As I have stated in the past, disqualifications are not enforcement remedies under the federal securities laws.[11] Waivers thus should not be used as bargaining chips in settlement negotiations, and neither I nor my staff consider waivers as a negotiable term when fashioning settlements. I am not aware of any instances in which the Enforcement Division staff has changed the language of a complaint to avoid triggering disqualifications necessitating a waiver.

Disqualifications guard against future participation in certain capital market activities by entities or individuals whose misconduct suggests that they cannot be relied upon to conduct those activities in compliance with the law and in a manner that will protect investors and our markets. The Commission enforces disqualifications in the same way it enforces other violations of the federal securities laws. When the Enforcement Division becomes aware of facts that suggest a possible violation has occurred—whether from a tip, complaint, referral, or other mechanism—it may institute an investigation into the conduct. In appropriate cases where there is sufficient evidence of a possible violation of the federal securities laws, the

[11] *See* Mary Jo White, Chair, SEC, Understanding Disqualifications, Exemptions and Waivers Under the Federal Securities Laws, Remarks Before the Corporate Counsel Institute (Mar. 12, 2015), https://www.sec.gov/news/speech/031215-spch-cmjw.html.

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Enforcement Division will recommend that the Commission bring enforcement actions against the alleged wrongdoers.[12]

Operation Broken Windows

In 2013, you announced Operation Broken Windows to prosecute small crimes on the theory that it will also deter more serious crimes. Knowing that the police implementation of Broken Windows Theory was flawed and led to distrust between African American and Latino communities and police, I am skeptical.

- **Do you believe this is the best way to deter and punish major frauds and other violations in our financial markets?**
- **Do you have any concrete evidence that this strategy is working?**
- **Isn't going after individual executives the single most important step you can take to ensure corporate accountability and an appropriate "tone from the top" that prioritizes compliance with the law?**

Response: I believe "Broken Windows," which is one of our enforcement tools, has been a great success, though it has frequently been misunderstood or mischaracterized. The strategy is not about turning every potential violation into an enforcement action. And it does not diminish the Commission's investigation and prosecution of major financial frauds. Instead, Broken Windows targets certain violations, such as control failures, negligence-based offenses, and strict liability-type violations, that involve important rules that have not been sufficiently complied with. We use a streamlined investigative and resolution process that provides incentives for violators to settle quickly. This has the effect of maximizing deterrence while conserving resources.

The success of Broken Windows is evidenced by the cases the Commission has brought. The Commission's initiative under Rule 105 of Regulation M of the Exchange Act, which prohibits firms from improperly participating in public stock offerings,[13] is a good example. The initiative uses streamlined procedures to achieve results and meaningful deterrence in an area that has not received significant enforcement attention in the past. To date, the Enforcement Division has filed three rounds of actions consisting of more than 150 alleged violations of Rule 105 by 50 respondents and defendants.[14] As a result, based on available

[12] For example, the Commission recently brought a settled action against an Australian financial services firm and its affiliates for continuing to engage in fund services activities after both the firm and its affiliates were disqualified from doing so as a result of an injunction entered against the firm by a federal district court in a separate case brought by the Commission. *See* Macquarie Capital Inv. Mgmt. LLC et. al., Investment Company Act Release No. 31706, Administrative Proceeding File No. 3-16676 (July 7, 2015), https://www.sec.gov/litigation/admin/2015/ic-31706.pdf.

[13] *See* 17 C.F.R. § 242.105. Rule 105 is an important rule that bans firms from improperly participating in public offerings soon after short selling those same stocks. The rule is intended to protect a stock offering from potential manipulation by short sellers who artificially depress market prices and, in the process, guarantee themselves a profit while reducing the company's offering proceeds and diluting shareholder value.

[14] *See* Press Release 2013-182, SEC, SEC Charges 23 Firms With Short Selling Violations in Crackdown on Potential Manipulation in Advance of Stock Offerings (Sept. 17, 2013),

information, the SEC has seen a significant decrease in Rule 105 violations since the initiative was announced in 2013. In the first fiscal year after the initiative was announced, Rule 105 violations, detected through various means available to the SEC, decreased significantly. Violations of Rule 105 in fiscal year 2015 were similarly lower than before the initiative.

I agree that the most effective deterrent is strong enforcement against responsible individuals, especially senior executives. Holding individuals accountable is a core principle of the Commission's enforcement program and we consider individual liability in every case. We have a strong record of holding individuals accountable. More than three-quarters of our cases over the last five years (excluding follow-on administrative proceedings and delinquent filings) have involved charges against individuals.

Conflicted Payments to Board Members

Today, some candidates for corporate boards enter into separate compensation arrangements with individual shareholders, whereby the shareholder agrees to 1) pay the candidate to get on the slate, 2) pay a salary to the candidate if they win, or both.

- **Given that, if elected, the candidate will have a fiduciary obligation to all shareholders, do such separate arrangements constitute a conflict of interest?**
- **Do proxy advisors disclose this information? Should they?**
- **Should these payments be prohibited?**

Response: The SEC does not regulate how directors are compensated, but rather requires clear and complete disclosure about such compensation. Whether such a payment would affect a director's fiduciary duty would be a question under state corporate law. Current SEC rules require the disclosure of all compensation awarded to, earned by, or paid to directors by any person for all services rendered in all capacities to the registrant and its subsidiaries in the registrant's annual report or proxy statement. Specifically, the disclosure of any payments to directors by these parties is required to be provided in the "All Other Compensation" column in the Director Compensation Table. In addition to this disclosure, current SEC rules require the disclosure of any arrangement or understanding between a director and any other person pursuant to which such director was selected as a director, which would include a supplemental or different compensation arrangement from the standard arrangement, identifying the director and describing the terms of that different arrangement.

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http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370539804376; Press Release 2014-195, SEC, SEC Sanctions 19 Firms and Individual Trader for Short Selling Violations in Advance of Stock Offerings (Sept. 16, 2014), http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370542963767; Press Release 2015-239, SEC, SEC Charges Six Firms for Short Selling Violation in Advance of Stock Offerings (Oct. 14, 2015), http://www.sec.gov/news/pressrelease/2015-239.html.

Proxy advisory firms state that they base their recommendations only upon publicly available information.[15] The SEC does not regulate what information must be considered or included when making recommendations about a particular security.

XBRL

This year the House Financial Services Committee passed the Small Company Disclosure Simplification Act (H.R. 1965). H.R. 1965 could cut off investors' access to searchable data for about 60% of public companies. Investors and the technology companies serving them need access to searchable data covering corporate financial performance. Documents that are non-searchable must be manually reviewed or expensively parsed to extract useful information which is unnecessarily time consuming, costly and prone to error.

- **If H.R. 1965 was to become law, what would the impact of exempting most public companies from reporting their financial information as searchable data in XBRL?**

__Response:__ In adopting rules to require the submission of financial statement information in XBRL format, the Commission considered, and requested comment on, exempting small companies from all or part of the requirements. After considering public comments, the Commission believed that a partial or complete exemption would detract from the long-term completeness and uniformity of the structured data format financial information database and would reduce the extent to which the amendments would enable investors and others to search and analyze the information dynamically.

Exempting a large number of issuers from filing their financial information in structured data format would undermine many of the benefits the Commission sought when it adopted the rules. If some portion of issuers were exempted, the Commission, investors, and analysts would have a diminished ability to evaluate the financial information of the exempted issuers, which may have a potential adverse impact on investor protection and the ability of the exempt issuers to raise capital in the public markets.

- **Do you think H.R. 1965 would damage efforts to modernize U.S. financial regulation?**

__Response:__ Yes. Access to significant amounts and types of data, both structured and unstructured, is vital to the Commission's work of regulating the U.S. capital markets. Machine-readable financial market data, including XBRL-formatted data, enhances the Commission's rulemaking and market monitoring activities because it allows staff to efficiently analyze large quantities of information. Without the ability to quickly and efficiently conduct statistical analyses of all SEC reporting companies, material gaps in

[15] *See ISS Draft Review Process for U.S. Issuers*, INSTITUTIONAL SHAREHOLDER SERVICES, https://www.issgovernance.com/iss-draft-review-process-u-s-issuers/ (stating that "ISS' proxy analyses are prepared using only publicly available information").

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market coverage could emerge that adversely impact the Commission's risk assessment initiatives and rulemakings.

- **It is my understanding that U.S. financial regulators lag behind the rest of the developed world in using modern data technologies to collect information from companies, financial firms, and markets. Is that true?**

Response: The Commission is committed to using modern technology to facilitate access to financial information. Technologies available to collect structured financial information can facilitate greater transparency, enable investors to easily search and analyze financial information, and facilitate comparison of financial performance across companies, reporting periods, and industries.

The Commission continues to work toward improving the transparency and accessibility of data that it requires entities to disclose. For example, the Commission recently adopted rules governing the security-based swap data repository ("SDR") registration process that require SDRs to provide their financial statements in XBRL format. The Commission has also proposed rules to specify the manner in which SDRs make security-based swap data available to the Commission, including proposed requirements that the data be made available according to schemas that will reference two industry-recognized standards for representing security-based swap data—the Financial products Markup Language ("FpML") standard and the Financial Information eXchange Markup Language ("FIXML") standard. The Commission has also proposed rules to modernize the reporting and disclosure of information by registered investment companies. The proposed rules include requirements that certain information, including information about portfolio holdings and census-type information, be reported in a structured data format.

Although other regulators may also use other data technologies to collect financial information, I believe the Commission has consistently incorporated the use of various forms of modern data technologies to collect and analyze financial information where appropriate.

- **Senators Mark Warner and Mike Crapo, and Commissioners Stein and Piwowar have all expressed support for the SEC to implement Inline XBRL so that public companies can report their financial statements just once, in a form that is both machine-readable and human-readable, rather than twice, once as plain text, then again as XBRL data, as they do today. What progress is the SEC making in following these recommendations?**

Response: In June, the Commission issued an order allowing companies to voluntarily file structured financial statement data using Inline XBRL. Use of an inline format may help to improve the quality of structured disclosures, ease filer burden, and facilitate review by staff, preparers, and investors by enhancing the ability to view XBRL enabled analytics and rendered XBRL data within the core filing. The experience and feedback received from the use of this option could facilitate the development of Inline XBRL preparation and analysis tools, provide investors and companies with opportunities to evaluate its usefulness, and help inform future Commission rulemaking in this area.

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Congressman Scott Garrett
Questions for the record for Full Committee hearing entitled "Examining the SEC's Agenda, Operations, and FY 2017 Budget Request"
November 18, 2015

1. **Chair White, during your appearance on November 18th, I asked you a series of questions regarding SIPC coverage and the circumstances that would decide whether investors are covered or not covered under the SIPA statute.**

    - **In your response, you stated coverage eligibility under SIPA would depend on actions taken by broker. Specifically, if a customer placed an order for $2,000 worth of stock and the broker actually went out and purchased the shares, the customer would have coverage under SIPA so long as they held any amount of those original shares. Separately, you explained that if the broker *did not* actually buy the shares because they were committing fraud or running a Ponzi scheme, an investor would not be covered under SIPA. Do I understand that distinction accurately, and if so, can you please provide further explanation as to why that is?**

Response: In 1970, Congress enacted SIPA in response to broker-dealer failures in the late 1960s in which many customers were either unable to recover their securities or cash or did so only after substantial delay. SIPA is designed to protect the custodial function of a broker-dealer in the event the firm is liquidated in a formal proceeding.[16] SIPA establishes procedures for broker-dealer liquidations and provides customers with special protections. The term *customer* is defined in SIPA to mean, in pertinent part: (1) a person who has a claim on account of securities received, acquired, or held by the broker-dealer in the ordinary course of its business as a broker-dealer from or for the securities accounts of such person for safekeeping, with a view to sale, to cover consummated sales, pursuant to purchases, as collateral, security, or for purposes of effecting transfer; or (2) any person who has deposited cash with the broker-dealer for the purpose of purchasing securities.[17]

In a SIPA liquidation, a fund of customer property is established for priority distribution to customers ahead of all other creditors. Each customer is entitled to a pro rata share of the customer property to the extent of the customer's net equity. *Net equity* is defined in SIPA to mean the dollar amount of a customer's account, determined by calculating, among other things, the value of all securities positions of the customer on the filing date of the liquidation proceeding and subtracting any amounts owed by the customer.[18] SIPA provides that, after receipt of a written statement of claim from a customer, the trustee shall promptly discharge all obligations of the broker-dealer to the customer relating to, or net equity claims based upon, securities or cash by delivery of securities or making payments to or for the account of

[16] *See SEC v. SIPC (In re Stanford Group Company)*, 758 F.3d 357, 362-63 (D.C. Cir. 2014) ("[SIPA] . . . protect[s] the custody function of brokers, *i.e.* by 'protecting customer interests in securities and cash left with broker-dealers.'").
[17] *See* 15 U.S.C. § 78*lll*(2)(B)(i)-(ii).
[18] *See* 15 U.S.C. § 78*lll*(11).

the customer insofar as such obligations are ascertainable from the books and records of the broker-dealer or are otherwise established to the satisfaction of the trustee.[19] If the amount of customer property is insufficient to satisfy a customer's net equity claim through a pro rata distribution, SIPC advances money to satisfy the claim up to $500,000 per customer, of which up to $250,000 can be used to satisfy a claim for cash.[20]

SIPA provides protection for a customer who places an order to purchase a specific security even if the broker-dealer does not purchase the security but instead steals the money deposited by the customer. When a customer deposits cash with a broker-dealer for the purpose of purchasing securities and receives a confirmation from the broker-dealer that the securities have been purchased, the customer is entitled to SIPA protection for the securities identified in the confirmation. This includes a priority (i.e., ahead of all non-customer creditors) pro rata claim to customer property held by the broker-dealer. Further, to the extent the customer property is insufficient to return all the securities owed to the customer, SIPC will advance to the customer up to $500,000 for the securities claim. In this case where the customer deposited cash with the broker-dealer, placed an order to purchase a specific security, and received confirmation of the purchase, SIPA protection applies regardless of whether the broker-dealer actually purchased the security or whether the broker-dealer was committing fraud or running a Ponzi scheme.

If, under a similar circumstance, the customer never received confirmation from the broker-dealer that the securities were purchased, the customer would be entitled to SIPA protection with respect to a claim for cash. As with a securities claim, the customer has a priority pro rata claim to customer property held by the broker-dealer. Further, to the extent the customer property is insufficient to return all the cash owed to the customer, SIPC will advance to the customer up to $250,000. In this case where the customer deposited cash with the broker-dealer, SIPA protection applies regardless of whether the broker-dealer was committing fraud or running a Ponzi scheme.

- **If it is the case that investors are covered under SIPA when the broker behaves properly and buys the shares but *not* covered if the broker commits fraud, how is an innocent investor supposed to know whether their broker is acting in good faith? If the SEC or FINRA fail to detect and shut down a Ponzi scheme despite repeated warnings (as happened with Madoff), do you believe innocent investors should be protected from such a government failure? Do you believe that they should be afforded full coverage under SIPC if the government allows a fraud to continue for years, as happened in Madoff? Moreover, it seems that your interpretation of SIPA would allow for the protection of customers of a broker-dealer that was run so poorly it had to declare bankruptcy, but not for customers of a broker-dealer in which fraud was committed. Why shouldn't coverage be applied in both**

[19] *See* 15 U.S.C. § 78*fff*-2(b).
[20] *See* 15 U.S.C. § 78*fff*-3(a).

circumstances, particularly when we are talking about innocent investors that trust their statements are accurate?

<u>Response</u>: SIPA protects customers who invest in a Ponzi scheme operated by a broker-dealer where the customers do not place orders to purchase specific securities, such as in Madoff. In this case, the customer is entitled to a return of cash invested in the Ponzi scheme, minus the amount of cash withdrawn from the broker-dealer. This method of determining net equity is designed to equitably distribute customer property recovered by the trustee in the liquidation. In contrast, in cases where investors deposit cash for investment purposes with an entity other than a broker-dealer, the claims for the cash or investments purchased with the cash are generally not entitled to the protections provided by SIPA.

The SEC is charged with oversight of SIPC and ensuring, in particular, that customers receive the protections under SIPA to which they are entitled. SIPA is designed to protect the custodial function of broker-dealers (i.e., the return of cash or securities held by the broker-dealer). Consequently, when the broker-dealer steals, trades without permission, or otherwise loses an investor's securities, the investor is protected as a "customer" under SIPA. While expanding the scope of SIPA to protect customers whose claims against a broker-dealer do not involve the custodial function could benefit more investors who are harmed by the misconduct of a broker-dealer, it also would involve significant costs that ultimately might be passed on to all investors. Policy makers would need to weigh these benefits and costs.

- **Exactly what circumstances would allow for SIPC coverage for investors? What types of malfeasance would disqualify an investor from receiving SIPC coverage? How is "fraud" defined or interpreted under the SIPA statute and where is the line drawn between who gets coverage and who does not?**

<u>Response</u>: The term "fraud" is not defined or interpreted under the statute. The following examples illustrate the extent of SIPA coverage in various circumstances, including some situations involving fraud:

Assume that 30 years ago a customer used \$2,000 to purchase 100 shares of XYZ Corp at a price of \$20 per share. Over time, those shares increased in value and the customer sold 30 shares realizing proceeds of \$2,000, which the customer withdrew from the account. Assume further that the broker-dealer fails holding 70 shares for the customer collectively worth \$5,000 (or approximately \$71 per share). If these are the only positions in the account, the customer's net equity would be \$5,000 notwithstanding the fact that the customer recouped the original \$2,000 investment amount by selling 30 shares. Thus, on the filing date, the customer would be entitled to a pro rata share of the customer property equal to \$5,000. If the customer property recovered by the trustee does not include 70 shares of XYZ Corp, SIPA provides that the trustee shall, to the extent that the securities can be purchased in a fair and orderly market, purchase 70 shares of XYZ Corp to return to the customer (otherwise the customer will receive the filing date value of the securities in cash (i.e., $5,000)). If the amount of customer property recovered in the liquidation is insufficient to return the 70 shares (or their filing date cash value), SIPC would make a cash advance to the trustee to satisfy the claim in full. In this way, SIPA protects the custodial function of the broker-dealer (i.e., its obligation to return 70 shares of XYZ Corp to the customer) regardless of whether the value of the shares had increased.

SIPA also protects a customer who places an order to purchase a specific security even if the broker-dealer does not purchase the security. For example, assume a customer places an order to purchase 100 shares of XYZ Corp at a price of $20 per share for a total purchase price of $2,000 and the customer receives a confirmation showing the trade was executed. Assume further that the broker-dealer does not actually purchase the shares for the customer and instead steals the $2,000. If the broker-dealer fails, the customer's net equity would be $2,000 notwithstanding the fact that the broker-dealer did not purchase the securities, assuming the market value of the XYZ shares did not change. Thus, on the filing date, the customer would be entitled to a pro rata share of the customer property equal to $2,000. Further, as noted above, SIPA provides that the trustee shall, to the extent that the securities can be purchased in a fair and orderly market, purchase 100 shares of XYZ Corp to return to them to customer (otherwise the customer will receive the filing date value of the securities in cash (i.e., $2,000)). If the amount of customer property recovered in the liquidation is insufficient to return the 100 shares (or their filing date cash value), SIPC would make a cash advance to the trustee to satisfy the claim in full.

SIPA also provides protections to customers of a broker-dealer who invest in a Ponzi scheme operated by a broker-dealer where the customers do not place orders to purchase specific securities. However, courts have held that a customer's net equity amount in this circumstance can be determined by adding the amount of cash the customer invested in the scheme less any cash withdrawn.[21] This method of determining net equity is designed to equitably distribute customer property recovered by the trustee in the liquidation. Under this approach, if the customer invested $2,000 in the broker-dealer's Ponzi scheme and did not withdraw the cash, the customer's net equity would be $2,000. Alternatively, if the customer had invested and subsequently withdrawn $2,000 from the scheme, the customer's net equity would be $0 and the customer would not be entitled to a SIPA advance or a pro rata share of customer property. The customer with a net equity claim of $2,000 and the customer with a net equity claim of $0 could file general creditor claims against the broker-dealer's estate for compensation (in addition to any recoveries under SIPA) arising from the harms they suffered as a consequence of the Ponzi scheme.

In addition to protecting customers who have deposited cash with a broker-dealer engaging in a Ponzi scheme, SIPA also protects customers who are victims of unauthorized trading.[22]

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[21] *See In re Bernard L. Madoff Inv. Securities LLC*, 654 F.3d 229 (2nd Cir. 2011); *Focht v. Athens* (In re Old Naples Securities, Inc.), 311 B.R. 607 (M.D. Fla. 2002); *In re New Times Securities Services, Inc.*, 371 F.3d 68 (2nd Cir. 2003).

[22] *See, e.g., In re Adler Coleman Clearing Corp.*, 198 B.R. 70, 75 (Bankr. S.D.N.Y. 1996); *Fine v. Bear, Stearns & Co.*, 765 F.Supp. 824 (S.D.N.Y. 1991). *See also In re Great Eastern Sec., Inc.*, 2011 WL 1345152 (S.D.N.Y. Apr. 5, 2011) (citing *In re Klein, Maus & Shire*, 301 B.R. 408, 420-21 (Bankr. S.D.N.Y. 2003) (citing *In re Adler,*

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For example, assume a customer used $2,000 to purchase 100 shares of XYZ Corp at a price of $20 per share. Over time those shares increase in value to $7,000. Assume further that without the customer's authorization the broker-dealer sells the 100 shares of XYZ Corp and uses the $7,000 proceeds to purchase 10,000 shares of ABC Corp (a stock the broker-dealer is manipulating as part of a pump and dump scheme). After the purchase, the customer receives a confirmation showing the transaction and immediately sends an email to the broker-dealer complaining about the transaction. However, before the customer's complaint can be addressed, the broker-dealer fails and the price of ABC Corp collapses when the scheme unravels so that the shares are only worth collectively $100. In this case, the customer's net equity claim would be based on the value of 100 shares of XYZ Corp on the filing date of the SIPA liquidation (assume it is $7,000) and the trustee would be obligated to return to the customer 100 shares XYZ Corp (or cash equal to their filing date value of $7,000). Consequently, the customer would not be left with the 10,000 shares of ABC Corp.

- **If an innocent investor cannot rely upon SIPA or the SEC to protect them (as unfortunately was the case in Madoff), what steps would you recommend they take to protect themselves?**

Response: Protecting individual investors from fraud is one of the SEC's highest priorities. In addition to the hundreds of actions the SEC brings against persons and entities who harm individual investors, the SEC provides numerous resources to help investors better protect themselves from investment fraud. Those resources—including *Investor.gov* (the SEC's educational website dedicated to individual investors), hundreds of in-person events, numerous publications, social media platforms, and other communication channels—provide tangible steps investors can take to help protect against fraud. Those steps include:

- Conducting a background check of any person or firm offering an investment on the SEC's Investment Adviser Public Disclosure website, where a prospective investor can research the history of a particular financial professional, including any regulatory actions, violations, complaints and employment history relevant to a firm or a representative.

- Learning about and looking out for common signs or "red flags" of investment fraud, including high, guaranteed rates of return, promises of "no risk" investments, pressure to make an investment decision quickly, and investing with persons not licensed with a state or the SEC.

- Asking questions about any potential investments, including about the risks of the investment and the fees, charges, and expenses involved – and not investing in anything unless the investor understands the product, the risks, and the fees involved.

Coleman Clearing Corp., 198 B.R. 70, 75 (Bankr. S.D.N.Y. 1996))); *Schultz v. Omni Mut. Inc.*, 1993 WL 546671 (S.D.N.Y.1993).

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- Contacting our Office of Investor Education and Advocacy directly (including via email, webform, and telephone) with questions, concerns, or complaints.

More information about all of the above topics, and information about other relevant topics, is available at Investor.gov.

In addition, investors should always promptly and carefully review the trade confirmations and account statements their brokers send them. Investors should verify that the confirmations and statements properly reflect all cash deposits and withdrawals, securities purchases and sales, and securities holdings. If an error is discovered in a trade confirmation or account statement, the investor should immediately bring the error to the attention of the broker-dealer in writing (e.g., letter or email). A complaint not made in writing may compromise eligibility for SIPC protection. If timely trade confirmations or account statements are not received, the customer should contact the broker-dealer immediately. Investors should also keep a copy of any writings sent to the broker-dealer.

- **You also stated in response to my questioning that there may be some circumstances where a customer may lose SIPC coverage after withdrawing their initial investment. What duty does a broker have to notify customer that they are no longer entitled to SIPC coverage? What duty does the SEC have to notify that customer? What duty does FINRA have to notify that customer? What duty does SIPC have to notify such a customer?**

Response: SIPA always protects the custodial function of a broker-dealer to the extent of a customer's net equity claim (i.e., the value of cash or securities the broker-dealer is holding for the customer less any amounts owed by the customer to the broker-dealer as of the filing date of a SIPA proceeding). Customers do not lose SIPA protection with respect to securities and cash owed to them by a broker-dealer after withdrawing their initial investment. A customer whose securities are being held by a broker-dealer or who has cash on deposit with a broker-dealer for the purpose of purchasing securities continues to be entitled to SIPA protection irrespective of any withdrawals of securities or cash from the broker-dealer. Therefore, it would not be appropriate to notify customers of the loss of SIPA protection when they withdraw their initial investment. SIPC protection is not available, however, in the circumstance when the customers did not, in fact, have any further net equity as defined under SIPA after withdrawing the initial investment, even though the account statements sent to the customers fraudulently reflected additional securities purchased.

2. **Chair White at the end of October the SEC put out a press release explaining its Fiscal Year 2015 enforcement actions, which included a "record" number of independent actions as well as a number of what the SEC called "first-of-their-kind" enforcement proceedings. These figures are also included in the budget requests that the SEC sends to Congress.**

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As I am sure you are aware, a study done by a professor at Emory University *("Reporting Agency Performance: Behind the SEC's Enforcement Statistics")* and which has received a lot of attention reviewed 15 years of enforcement statistics published by the SEC and found that the *"SEC double and triple counts many of its cases and overstates the fines that it orders"* The study estimated that *"between 23% and 34% of SEC enforcement actions brought each year have already been counted at least once"*, meaning that the numbers published by the SEC every year could be grossly overstated.

- **Are you familiar with the study and if so, what if any particular aspects of the study do you dispute?**
- **If the SEC obtains a monetary penalty against an individual and then also bars that same individual or takes their license away, would that be counted as multiple enforcement actions in the statistics that the SEC publishes?**
- **So looking through the SEC's release from October, you state that the agency filed "807 enforcement actions" – were those 807 *unique* actions against different individuals?**
- **Have you found any inconsistencies at all in the way that the SEC reports enforcement statistics, and if so what steps have you taken to rectify them?**

Response: For FY 2015, the Commission filed 807 enforcement actions. Of the 807 enforcement actions, 507 were civil actions or stand-alone administrative proceedings for violations of the federal securities laws (a 23% increase from the prior year), 132 were administrative proceedings against issuers who were delinquent in making required filings with the SEC, and 168 were follow-on administrative proceedings seeking bars against individuals based on criminal convictions, civil injunctions, or other orders.[23]

The main thrust of the article referred to in your question is that based on the actual number of Commission actions, the Commission's enforcement activities have remained flat since 2002.[24] I completely disagree with that premise. The number and quality of our actions, the impact those actions have had on the markets, the significant increase in monetary penalties and disgorgement ordered in our cases (for example, the total penalties ordered in 2002 was $101 million compared to $1.2 *billion* in FY 2015), and other factors are evidence that our program has been increasingly effective in its enforcement of the securities laws.

The Commission has been consistent and transparent in reporting our enforcement statistics. Every fiscal year, the Commission tracks and reports the total number of enforcement actions filed and the total amount of financial remedies ordered, in addition to other statistics. The

[23] *See* SEC, SELECT SEC AND MARKET DATA FISCAL 2015 (Feb. 5, 2016), https://www.sec.gov/about/secstats2015.pdf.
[24] *See* Urska Velikonja, *Reporting Agency Performance: Behind the SEC's Enforcement Statistics*, 101 Cornell L. Rev. 901, 901 (2016).

total number of enforcement actions reported each year is exactly that—the total number of all enforcement actions filed during the fiscal year. It includes civil actions and stand-alone administrative proceedings for violations of the federal securities laws, administrative proceedings against issuers who were delinquent in making required filings with the Commission, and follow-on administrative proceedings seeking bars against individuals based on criminal convictions, civil injunctions, or other orders. As a result, if the Commission files a civil action against an individual for violating the federal securities law and obtains a civil injunction or other order against that individual, and then files a separate follow-on administrative proceeding against that individual, both of these proceedings will be counted in the total number of enforcement actions reported by the Commission. I believe that this is entirely appropriate, particularly given the importance of our bar remedies in protecting investors from fraud. As the article acknowledges, the Commission has reported these numbers in the same way for many years,[25] and all enforcement actions are disclosed in detail on the Commission's website (sec.gov) as they are filed. The Commission's reporting of its enforcement statistics for fiscal year 2015 provides, in addition to the total number of enforcement actions filed, a breakdown of the number of actions in each of the foregoing categories for fiscal years 2014 and 2015.[26]

The article incorrectly states that the Commission's reported monetary amounts include amounts "ordered but waived."[27] The Commission does not include amounts waived in its calculation of the total amount of monetary amounts ordered each year. The article also incorrectly suggests that a large portion of the penalties and disgorgement the Commission reports each year are jointly ordered in both Commission and parallel criminal cases, or other parallel cases with other regulators, and criticizes the Commission for including these amounts in its statistics. In fact, these amounts collectively represent only a relatively small percentage of the total amounts reported—averaging less than 7% over the last few years—and I believe are appropriate to include in the Commission's year-end totals because our investigations often assist and lead to criminal authorities and other regulators bringing cases.

I also disagree with the article's claim that the Commission views the number of enforcement actions as the most important measure of its enforcement activity.[28] While it is very important that the Commission's enforcement actions reflect the full spectrum of market participants and market misconduct, the quality of our enforcement actions is more important than the number of actions. In its reporting of enforcement statistics and other public statements, the Commission and its staff stress that that numbers only tell a small part of the story and that what makes our enforcement program a success is the breadth and impact of

[25] In fiscal year 2013, the Commission narrowed its definition of contempt actions included in its total number of enforcement actions. The Commission also omitted 21(a) Reports in its enforcement action results. These changes did not have a material effect on the total number and, if anything, resulted in fewer total actions reported.
[26] *See* SEC, SELECT SEC AND MARKET DATA FISCAL 2015 (Feb. 5, 2016), https://www.sec.gov/about/secstats2015.pdf.
[27] *See* Urska Velikonja, *Reporting Agency Performance: Behind the SEC's Enforcement Statistics*, 101 Cornell L. Rev. 901, 948 (2016).
[28] *See id.* at 939-940.

our actions.[29] This includes bringing actions that address meaningful issues for investors and the markets, filing actions that span the securities industry, bringing first-of-their-kind actions, and providing a strong deterrent to would-be violators.

I do not believe there are inconsistencies in the way that the SEC reports enforcement statistics. I expect that we will continue to provide the same categories of information in our enforcement statistics going forward.

3. **Chair White, as I've said before I commend you for undertaking a review of our equity market structure in a holistic and data-driven manner. However, I remain concerned that progress on this project seems to have stalled a bit and it's unclear to me what the next steps are.**

    - **What is the current status of this project and what further initiatives or rulemakings do you anticipate undertaking over the next year?**

Response: The SEC's comprehensive review of market structure remains a top priority, and the Commission continues to proceed with its ongoing assessment of U.S. equity market structure. As I have previously stated, one of the guiding principles of our market structure review is the need to ground market structure assessments in empirical evidence. The Commission has a website devoted exclusively to equity market structure, located at https://www.sec.gov/marketstructure. The website is intended to serve as a central location to publicly share data, research, and analysis related to equity market structure and to provide the public a forum to review the information. The SEC staff continues to share its analysis of equity market structure issues by publishing on the website data highlights and research papers that address many of the most pressing market structure questions, including the speed of trading, order cancellations, high frequency trading, market fragmentation, off-exchange trading, market quality for small cap stocks, volatility, and the operation of our equity markets under the stressed market conditions of August 24, 2015.

In addition, in February 2015, the Commission established the Equity Market Structure Advisory Committee to provide a formal mechanism through which the Commission can receive advice and recommendations on equity market structure issues. The first meeting, held on May 13, 2015, focused on Rule 611 of Regulation NMS, known as the "Order Protection Rule" or "Trade-Through Rule." The second meeting, held on October 27, 2015, focused on two important market structure topics: 1) the impact of access fees and rebates

[29] *See e.g.*, Press Release 2015-245, SEC, SEC Announces Enforcement Results For FY 2015 (Oct. 22, 2015), http://www.sec.gov/news/pressrelease/2015-245.html; Mary Jo White, Chair, SEC, Examining the SEC's Agenda, Operations and FY 2017 Budget Request, Testimony Before the Committee on Financial Services, U.S. House of Representatives (Nov. 18, 2015), http://www.sec.gov/news/testimony/chair-white-testimony-sec-agenda-operations-2017-budget.html ("More important than the numbers, these actions addressed meaningful issues for investors and markets, spanned the securities industry, and included numerous 'first-of-their-kind' actions."); Andrew Ceresney, Dir., Div. of Enf't, SEC, *Remarks to the American Bar Association's Business law Section Fall Meeting* (Nov. 21, 2014), http://www.sec.gov/News/Speech/Detail/Speech/1370543515297 ("But as I always say, numbers only tell a small part of the story. What made our year particularly noteworthy was the breadth and impact of our actions.").

widely used by securities exchanges; and 2) the regulatory structure of trading venues. Following the second meeting, the Committee established subcommittees to look more closely at specific issues before presenting them to the full Committee for discussion and deliberation. The third meeting was held on February 2, 2016, and focused on the events of August 24, 2015, and certain issues affecting customers in the current equity market structure. The fourth meeting was held on April 26, 2016 and focused on a recommendation for a potential Access Fee Pilot framework and recommendations relating to trading venues regulation; recommendations in both areas were approved by the Committee in a July telephonic meeting and transmitted to the Commission for its consideration. The sixth meeting, held on August 2, 2016, focused on recommendations related to market quality and customer issues, as well as updates from the subcommittees.

In addition to the efforts noted above, we have progressed on the rulemaking initiatives I publicly announced in 2014, targeting specific aspects of market structure that may be working against the interests of investors and issuers. These rulemakings afford the Commission the opportunity to evaluate and assess in detail specific aspects of our equity market structure through the public rulemaking process. Specifically:

- On March 25, 2015, the Commission proposed amendments to Rule 15b9-1 to require broker-dealers that engage in off-exchange proprietary trading to become members of a national securities association. As proposed, the rule would improve regulatory oversight of active proprietary trading firms, such as high-frequency traders. Staff is reviewing comment letters received on the proposal and preparing a final recommendation for Commission consideration.

- On May 6, 2015, the Commission approved the initiation of a pilot on different tick sizes, which will test the impact of wider quoting and trading increments on the liquidity and trading of certain smaller capitalization companies for a two-year period. The Commission plans to use the pilot program to assess whether wider tick sizes enhance the market quality of these stocks for the benefit of issuers and investors. The pilot began on October 3, 2016.

- In November 2015, the Commission proposed amendments to Regulation ATS to expand the information that alternative trading systems ("ATSs") disclose to the Commission about their operations and, for the first time, would require ATSs to make operational information available to the public. The comment period expired on February 26, 2016. Staff is considering all comment letters received and progressing towards a recommendation for Commission consideration.

- In April 2016, the Commission voted to publish for public comment a proposed national market system ("NMS") plan to create a single, comprehensive database that would enable regulators to efficiently track all trading activity in the U.S. equity and options market. The comment period for this plan to create the consolidated audit trail closed on July 18, 2016, and the staff is working on preparing a recommendation for the Commission's consideration. There is no higher market structure priority for me in 2016 than to ensure Commission consideration of the final CAT plan before the end of the year.

- In July 2016, the Commission proposed rules that for the first time would require broker-dealers to disclose the handling of institutional orders to customers. The proposed rules also would expand the information included in existing retail order disclosures. The comment period closed on September 26, 2016.

I am pleased with the staff's focus on these initiatives to date and look forward to continued progress on these and other efforts in the months ahead.

- **During your review, have you identified specific areas or issues within our equity markets that the SEC should dedicate more resources to? If so, what are those issues?**

Response: The Commission's Division of Trading and Markets ("TM") and Division of Economic and Risk Analysis ("DERA") devote significant resources to oversight of the U.S. equity markets. This oversight is conducted by staff across offices that are dedicated to the administration of broker-dealer conduct, trading, and financial responsibilities rules; oversight of clearing requirements and risk management; oversight of trade reporting; and also the development of new initiatives on improved price transparency in the securities markets, among other things. The Commission will continue to focus on the execution of our core programs and operations by seeking to hire individuals with the skill sets necessary to enhance the agency's oversight of increasingly complex securities markets; striving to build the significant new oversight programs assigned to the Commission in recent years; and continuing to enhance our technology, including our ability to analyze and assess large volumes of data.

- **The Capital Markets Subcommittee held a hearing on the impact of Reg NMS back in 2014 – are you committed to analyzing the impacts of Reg NMS on all market participants as you have said you would do in the past?**

Response: The Commission continues to proceed with its ongoing assessment of U.S. equity market structure, including Regulation NMS. In addition to the staff's analysis of the rules affecting equity market structure, and its empirical analysis of our current equity markets, the Commission's Equity Market Structure Advisory Committee has been considering Regulation NMS. At the inaugural meeting, the Committee focused on Rule 611 of Regulation NMS and discussed the impact of trading centers' policies and procedures designed to prevent "trade-throughs." At the second meeting, the Committee focused on Rule 610 of Regulation NMS. Specifically, the Committee discussed the impact of the access fees and rebates that today are widely used by exchanges and other trading venues.

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In addition, the Committee has formed subcommittees on the following four topics: Regulation NMS, trading venues regulation, customer issues, and market quality. The first subcommittee will consider the causal effects of Regulation NMS and its four main components (i.e., the Order Protection Rule, Access Rule, Sub-Penny Rule, and Market Data Rule) on equity market structure in the U.S. This subcommittee is charged with examining the impact of Regulation NMS and whether the rules should evolve with the changes in trading technology, practices, and competition. For example, in June, the Regulation NMS subcommittee published a proposed recommendation for the Committee's consideration regarding an access fee pilot to determine the impact of exchange access fees and rebates on our equity market structure. The full Committee voted in July to send a revised version of that recommendation to the Commission for its review. The Commission looks forward to receiving other recommendations from the Committee on issues related to Regulation NMS.

In dialogue with the Committee and otherwise, the staff has been reviewing aspect of Regulation NMS and making recommendations where appropriate. For example, the Commission recently proposed amendments to update investor disclosures under Rules 605 and 606, central components of Regulation NMS designed to ensure investors have the information they need about how their orders are handled. Similarly, the Commission ordered the implementation of a pilot program—which began operating on October 3—to study increases in the minimum "tick size" for equity trading, another important component of Regulation NMS.

4. **How has the recent 2nd Circuit decision in *U.S. v. Newman*, for which the Supreme Court recently refused to grant cert, affected the Commission's ability to bring insider trading cases?**
   - **How has the Division of Enforcement shifted its priorities or resources in light of the *Newman* decision?**
   - **Notwithstanding the *Newman* decision, does the Commission have adequate statutory authority to bring enforcement actions for insider trading violations?**
   - **SEC's New York Regional Office Director, Andrew Calamari, recently responded to questions about how the *Newman* decision would hinder the SEC's ability to obtain insider trading convictions, stating that "we haven't changed a thing." Calamari continued that despite *Newman*, "[m]any of your insider trading cases are not multiple layers removed from the source. So a lot of issues Newman raises, the complexities seemingly raised by Newman, probably are not going to be there." Are these comments consistent with your views?**

Response: *Newman* is undoubtedly an important case, but I think the extent of its impact on the Commission's insider trading cases has been overstated by some commentators. It's ultimate impact remains to be seen. The Commission has a very impressive record pursing insider trading in recent years and has continued to be aggressive since *Newman* was

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decided.[30] We have seen courts within the Second Circuit narrowly construe *Newman*'s broadest implications.[31] In addition, the Supreme Court recently granted *certiorari* in *U.S. v. Salman* from the Ninth Circuit, and its decision in that case will likely address the personal benefit issues raised in the *Newman* decision.[32]

Since *Newman*, we have focused closely on personal benefit in our insider trading investigations. Going forward, we will continue to be aggressive in bringing insider trading cases, while mindful of the potential impact of *Newman* on our investigations.

Strong insider trading laws are essential to the Commission's ability to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation. In my view, it would be valuable to gain further experience from the Commission's enforcement program on the impact of *Newman* and further development of the case law, including the Supreme Court's decision in *Salman*, to help evaluate whether, and what type of, additional statutory or regulatory changes related to insider trading may be appropriate.

5. **In the SEC's adopting release for its CEO pay ratio rule, it estimated that the compliance costs for companies would $1.3 billion on an upfront basis, and $526 million on an ongoing annual basis. Yet, the potential benefits provided by the rule were unclear – with the adopting release noting the SEC's "inability to quantify the benefits." Chair White, can you explain the benefits of the CEO pay ratio rule?**

    a. **Why was the SEC staff unable to quantity the benefits? Am I to conclude that there are no quantifiable benefits?**

Response: As explained in the adopting release, the Commission believed that the pay ratio disclosure provides information that shareholders may find relevant and useful when exercising their say-on-pay voting rights. Various commenters stated that they would find

[30] The Commission has charged more than 650 defendants in civil insider trading cases over the last six years and has filed more than 40 insider trading cases since *Newman* was decided in December 2014.
[31] *See, e.g., SEC v. Payton*, 97 F. Supp. 3d 558, 560 (S.D.N.Y. 2015) (holding that SEC had sufficiently alleged personal benefit under *Newman* where defendants were roommates who "shared a close mutually-dependent financial relationship, and had a history of personal favors"); *SEC v. Payton*, 155 F. Supp. 3d 428, at 431-434 (S.D.N.Y. 2015) (denying defendants' motion for summary judgment); *SEC v. McGinnis*, No. 14-cv-6, 2015 WL 5643186, at *18-*20 (D. Ver. Sept. 23, 2015) (denying defendants' motion for summary judgment where a reasonable jury could conclude that there was a personal benefit under *Newman* where the tipper and tippee shared a "close business relationship" that also included an "exchange of information"). *See also SEC v. Andrade*, 197 F. Supp. 3d 124, at 126-130 (D. R.I. 2016) (holding that the SEC had sufficiently alleged personal benefit where the tipper and tippee's "relationship where there was, at a minimum, a give and take of sorts that had the potential for pecuniary gain").
[32] In *United States v. Salman*, 792 F.3d 1087 (9th Cir. 2015), the Ninth Circuit rejected the defendant's request to adopt a broad reading of *Newman* and confirmed that "personal benefit is broadly to include not only pecuniary gain, but also, *inter alia*, . . . the benefit one would obtain from simply making a gift of confidential information to a trading relative or good friend." 792 F.3d at 1093-94 (quoting *Newman*, 773 F.3d at 452). Salman appealed this decision challenging the Ninth Circuit's definition of personal benefit and the Supreme Court granted *certiorari* on January 19, 2016. *See Salman v. United States*, 136 S.Ct. 899 (Jan. 19, 2016).

the pay ratio disclosure relevant when making voting decisions; however, those commenters did not provide specific data or suggest a source of data or a methodology that the Commission could use to quantify the potential benefits.

The Commission was unable to quantify the benefits for several reasons. First, the primary benefit of the disclosure is not directly tied to an immediate economic transaction, such as the purchase or sale of a security. Second, the pay ratio disclosure is one data point among a number of considerations that shareholders might find relevant when exercising their say-on-pay votes. Third, because the say-on-pay vote is advisory and not binding, it is difficult to link the disclosure with certainty to changes in the principal executive officer's compensation or economic outcomes at a registrant. The Commission's and commenters' inability to quantify benefits does not indicate that there are no benefits to this rule.

b. How do those benefits outweigh the substantial costs?

Response: As noted above, the Commission could not quantify the benefits of the final rule. As explained in the adopting release, the Commission believed it reasonable to rely on Congress's determination that the rule will produce benefits for shareholders and that its costs are necessary and appropriate in furthering shareholders' ability to meaningfully exercise their say-on-pay voting rights. Because Congress expressly directed the Commission to undertake this rulemaking, the Commission did not believe it would be appropriate to second-guess Congress's apparent conclusion that the benefits from this rule justify its adoption. The Commission also explained in the adopting release that it was Congress' judgment that the pay ratio disclosure could be beneficial for shareholders.

c. Why did the SEC fail to use its substantial discretion to remove certain classes of employees, such as foreign employees, from the final rule?

Response: The Commission believed that excluding broad categories of employees would not be consistent with the statutory language of Section 953(b), which referred to "all employees," or with the purpose of providing a company-specific metric that shareholders can use to evaluate a registrant's executive compensation. In addition, the Commission indicated that including both U.S. and non-U.S. employees will result in pay ratio disclosure that reflects the actual composition of the registrant's workforce.

To help address concerns about compliance costs, the final rule allows the use of statistical sampling and reasonable estimates, generally requires that the median employee be identified only once every three years, and provides for *de minimis* and foreign data privacy exemptions, among other things.

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HFSC Hearing entitled "Examining the SEC's Agenda, Operations, and FY 2017 Budget Request"
Mary Jo White, Chair, Securities and Exchange Commission
November 18, 2015

Questions for the Record from Congressman Hultgren (R-IL)

Under Section 31 of the Securities Exchange Act of 1934, national securities exchanges and other self-regulatory organizations owe proportional transaction fees to the Securities and Exchange Commission (SEC) for the cost of supervising and regulating such transactions. There are circumstances where these fees may be unintentionally overpaid; however, the SEC has maintained they lack the legal authority to reimburse such fees.

1. **What options does the SEC have, without a change to the Securities Exchange Act of 1934, to return these overpaid fees?**
2. **What is the last time the SEC reassessed its legal authority to reimburse Section 31 fees? Has its position changed since a May 15, 2013, letter to the Chairman of the House Financial Services Committee which requested clarification of its authority? If so, is there new information or an updated legal opinion upon which it is relying?**
3. **What options does the SEC have, without a change to the Securities and Exchange Act of 1934, to reimburse overpaid Section 31 fees, if any?**

Response: SEC staff remains in discussions with staff at OMB and Treasury concerning the SEC's authority to return overpaid fees made under Section 31. Based on these discussions, it does not appear that the SEC has authority to offset past years' overpayments against future years' payments. This is because the SEC is required by statute to collect as much in Section 31 fees as is necessary to reimburse the amount Congress has appropriated to the SEC for that fiscal year. Reimbursing from a current fiscal year for payments associated with a prior fiscal year would cause the appropriation to the SEC to be unreimbursed in the amount of such refunds. Such a result would appear to be contrary to statutory direction to the SEC to establish a Section 31 fee rate that "is reasonably likely to produce aggregate fee collections . . . equal to the regular appropriation to the Commission by Congress for such fiscal year." Exchange Act, Section 31(j)(1). It thus appears that this course of action would require new legislation. Nonetheless, SEC staff continues to work with OMB and Treasury staff to determine if there is a mechanism for refunding or paying requests from prior years' Section 31 payments, where appropriate, without need for further legislation.

4. **Has the SEC ever reimbursed overpaid Section 31 fees? If so, please provide the date and amount of these reimbursements.**

Response: According to our records, in January 2011, the SEC issued a reimbursement to NYSE Arca, Inc. for an $802,478 overpayment made by the entity when it was operating as the Pacific Exchange, Inc. Since that time, SEC staff has been consulting with OMB and Treasury staff on the scope of the legal authority in this area.

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Also, before 2004, there were historical instances of SROs that performed offsets on their own without SEC objection. In 2004, the SEC adopted a new Rule 31 to enhance internal controls over Section 31 fees by establishing tighter procedures for the calculation and collection of these fees. These improved procedures had the effect of making such offsets no longer possible.

5. **What is the amount of overpaid Section 31 fees currently held by the SEC they are unable to reimburse?**

Response: SEC staff is currently aware of outstanding requests that total approximately $3.4 million. This amount may fluctuate as SROs work to assemble additional documentation about such requests in response to the SEC staff's recent letters to the refund requesters.

6. **Does the SEC have any plans to spend overpaid Section 31 fees other than reimbursement?**
7. **Are there any other examples of the SEC being unable to provide reimbursement for an overpayment?**

Response: The SEC has no intention of spending (or ability to spend) any past overpayments for other purposes. SEC staff is not aware of any other examples of the SEC being unable to process a reimbursement for overpayment.

Section 913 of the Dodd-Frank Act granted the SEC authority under the Exchange Act and Advisers Act to adopt rules establishing a uniform fiduciary standard of conduct for broker-dealers and investment advisers when providing personalized investment advice about securities to retail customers.

1. **In general, what are your thoughts on the concept of limiting the types of investments that can be held in retirement accounts?**
2. **Given your knowledge of the financial services marketplace, do you think limiting the assets that can be held in retirement accounts is in the best interest of people saving for retirement?**

Response: I believe that broker-dealers and investment advisers should be subject to a uniform fiduciary standard of conduct when providing personalized investment advice about securities to retail investors. I fully recognize, however, that this is a very complex issue, and that there are many challenges that will need to be addressed in proposing a uniform fiduciary standard, including how to define the standard, how it would affect current business practices, and the nature of the potential effects on investors.

I also recognize that implementation of a uniform fiduciary standard must consider the potential economic and market impacts, including consequences that may result for investors and market participants, and any proposal would include a robust economic analysis. Any action we take in this area would take into account related concerns, such as a potential reduction in availability of advice or services. In addition, any Commission proposal would solicit public comments to better inform our efforts. It is important that the Commission strike the right balance in addressing these issues while making sure investors, particularly retail investors, are appropriately protected and have access to the type of investment advice they need and can afford.

During a November 18, 2015, hearing before the House Financial Services Committee on *Examining the SEC's Agenda, Operations, and FY 2017 Budget Request* you testified, "I also participated in some meetings with Secretary Perez to provide technical assistance and expertise from our space to them, some -- our sense of -- our economists met with them on a number of the issues." On Friday, March 6, Secretary Perez told CNBC that "I've personally met a number of times with Chairwoman White" and "Our staffs have been working closely throughout."

1. **During these meetings, what was the Department of Labor's explanation for limiting the use of listed options in retirement accounts? Did DOL request input from the SEC on this matter?**

2. **The Department of Labor's proposal mentions annuities 172 times but the Regulatory Impact Analysis does not examine the impact of the rule on annuities, advisers, insurers, or the retirement savers using them. Given your role as a regulator for insurance products, what impact analysis did you share with the Department of Labor regarding its treatment of annuities?**

3. **What economic analysis has the SEC provided to the Department of Labor?**

4. **What are some specific examples of input from the SEC that Labor has used in its public proposals?**

Response: I met with Secretary Perez in person several times and we spoke over the phone about the DOL's fiduciary rulemaking. Commission staff also provided technical assistance in connection with DOL's rule. Specifically, Commission staff met with staff from DOL on a number of occasions, providing technical expertise regarding the regulation of investment advisers and broker-dealers, including disclosure requirements and our approach to the conflicts that surround, among other things, principal trading, differential compensation, and receipt of commissions. SEC staff also provided technical expertise on other topics during the rulemaking process, including swaps, listed and unlisted options, and annuities. On occasion, Commission staff economists also discussed with DOL staff economists cost-benefit related issues as well as relevant academic literature.

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The DOL and the SEC are two separate agencies with separate statutory mandates, and ultimately DOL determined what changes to incorporate in the final rule. As is the case with any rule, changes were made throughout the rulemaking process.

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Questions for the Record for Honorable Mary Jo White
Chair of the Securities and Exchange Commission
Submitted by Congressman Robert Hurt (VA-05) on December 3, 2015
"Examining the SEC's Agenda, Operations, and FY 2017 Budget" November 18, 2015

1. **What specifically can and should be changed in the NMS governance space with regard to having broker dealer representation on the operating committees of the NMS plans? Why should NMS plan participants solely be from the Self-Regulatory Organizations (SROs), what challenges or hurdles would be presented if broker dealers were added to the operating committees and had voting representation on such committee, and what liabilities would be added for the SROs if broker dealers are added to the operating committees?**

2. **During my questioning on November 18, 2015, you suggested that having representation from the industry on the Operating Committees would not impair the operating functionality of the systems. Does that mean that you are suggesting that having broker dealer representation would not impair NMS Plan's functions and would not impair the functionality of the Operating Committees?**

4. **Can you provide specifics on the SRO's rights and liabilities under Section 11A of the Securities and Exchange Act of 1934 and how adding broker dealer representation to the Operating Committees of the NMS Plans would impact the SRO's rights and liabilities, and whether such new additional broker dealers would be exposed to any additional rights and obligations by virtue of being on the operating committees. Does the Commission believe that it has the existing statutory authority to amend the NMS governance structure? Are their plans for the SEC to do so? Can the Commission accomplish a governance structure and reform to NMS governance apart from comprehensive market structure reform?**

Response: By way of background, Section 11A of the Securities Exchange Act of 1934 ("Exchange Act") directs the Commission to facilitate the establishment of a national market system for securities.[33] In so doing, the Commission, by rule or order, may authorize or require the SROs to act jointly with respect to matters as to which they share authority in planning, developing, operating, or regulating the national market system or facility thereof.[34] Pursuant to Rule 608 under Regulation NMS,[35] the Commission may authorize any two or more SROs, acting jointly, to file an NMS plan with respect to the operation of a national market subsystem or facility. Rule 608 requires each SRO to comply with the terms of any effective NMS plan for which it is a sponsor or participant and to enforce compliance (absent reasonable justification or excuse) with any such plan by its members and their associated persons.[36] Any NMS plan filed with the Commission is published for public comment, and no NMS Plan becomes effective unless approved by the Commission or

[33] 15 U.S.C. § 78k-1.
[34] See Exchange Act Section 11A(a)(3)(B), 15 U.S.C. § 78k-1(a)(3)(B).
[35] 17 C.F.R. § 242.608.
[36] See Regulation NMS Rule 608(c), 17 C.F.R. § 242.608(c).

otherwise permitted by Rule 608.[37] The NMS plans in effect today include those that provide for: (1) the collection and dissemination of consolidated market data;[38] (2) the operation of the limit up-limit down plan to address extraordinary market volatility;[39] (3) the linkage of the options markets and their surveillance;[40] and (4) the operation of the tick size pilot.[41] In addition, the Commission has published for comment an NMS Plan regarding a proposed consolidated audit trail.[42]

Several NMS plans today require the creation of an advisory committee composed of broker-dealer representatives, among others, that have the right to attend meetings of the operating committee and provide their views to the SROs.[43] In recent years, broker-dealers have expressed concern about the effectiveness of their participation in NMS plan governance and the viability of the advisory committee mechanism. Some have advocated that representatives of broker-dealers and other market participants be given full voting membership on NMS plan operating committees.

NMS plan governance is one of the many important topics the Commission currently is assessing as part of its broad-based review of equity market structure. In fact, the Commission's Equity Market Structure Advisory Committee ("EMSAC")[44] has been

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[37] See Regulation NMS Rule 608(b), 17 CFR § 242.608(b).

[38] The CTA/CQ Plans govern the collection, processing and distribution of quotation and transaction information for equity securities listed on all exchanges other than Nasdaq. For more information on these plans, see https://www.ctaplan.com/index. The Nasdaq UTP Plan governs the collection, processing and distribution of quotation and transaction information for securities listed on Nasdaq. For more information on this plan, see http://www.utpplan.com/DOC/UTP_Plan.pdf. In addition, the Options Price Reporting Authority ("OPRA") Plan provides for the collection and dissemination of last sale and quotation information on options that are traded on the participant exchanges. For more information on this plan, see http://www.opradata.com.

[39] The NMS Plan to Address Extraordinary Market Volatility ("LULD Plan") provides for a market-wide limit up and limit down mechanism designed to prevent trades in NMS stocks from occurring outside of specified price bands, coupled with trading pauses to accommodate more fundamental price moves. For more information on this plan, see http://www.finra.org/industry/trf/limit-uplimit-down-luld-plan#sthash.PvVhnRD5.dpuf.

[40] The Options Order Protection and Locked/Crossed Markets Plan requires the options exchanges to establish a framework for providing order protection and addressing locked and crossed markets in eligible options classes. For more information on this plan, see http://www.optionsclearing.com/components/docs/clearing/services/options_order_protection_plan.pdf.

[41] The Plan to Implement a Tick Size Pilot Program would widen the quoting and trading increments for certain smaller-capitalization stocks. For more information on this plan, see https://www.sec.gov/divisions/marketreg/tick-size-pilot-plan-final.pdf.

[42] The Consolidated Audit Trail Plan ("CAT Plan") is proposed to capture customer and order event information for orders in NMS securities, across all markets. *See* Notice of Filing of the National Market System Plan Governing the Consolidated Audit Trail, Exchange Act Release No. 77724 (Apr. 27, 2016), https://www.sec.gov/rules/sro/nms/2016/34-77724.pdf.

[43] *See* CTA/CQ Plans, Nasdaq UTP Plan, LULD Plan and proposed CAT Plan.

[44] The Commission established the EMSAC to provide the Commission advice and recommendations on equity market structure issues. The Commission has encouraged the EMSAC to consider, among other issues, whether various regulatory or industry initiatives would improve the function of the U.S. equity markets. As an advisory committee to the SEC, EMSAC is organized and operates pursuant to the Federal Advisory Committee Act, 5 U.S.C. app. §§ 1-16. *See* Equity Market Structure Advisory Committee, SEC.gov, https://www.sec.gov/spotlight/equity-market-structure-advisory-committee.shtml.

reviewing this issue, and recently issued specific recommendations at its July 8, 2016 meeting. Those recommendations include expanding the role of NMS plan advisory committees to provide them a formal vote on any matter on which the operating committee votes, as well as to initiate their own recommendations to the operating committee.[45] We are evaluating these recommendations.

It is important to bear in mind that NMS plans serve important regulatory purposes, such as ensuring that accurate and reliable consolidated market data is widely available to investors, that our markets have robust mechanisms to protect against excessive volatility, and that SROs can effectively surveil the markets. At the same time, I recognize the importance of incorporating the views of broker-dealers and other stakeholders in the operation of an NMS plan at an early stage of the decision-making process. Early stage engagement may, among other things, enhance the quality of the proposals developed by the NMS plans as well as facilitate more swift adoption and implementation. Accordingly, enhancements to the governance of NMS plans designed to ensure that the views of key stakeholders are taken into account are worthy of serious consideration. The Commission has existing authority to take action in this area.

3. **Chair White, do you believe that a conflict of interest exists in the current governance structure of NMS Plans, specifically having the SROs run the plans and also being beneficiaries of the Plans? Can you provide comments on the current conflicts of interest of having the NMS plans being run by the SROs and then the SROs offering competing products from those which are being directed by the Plans? Specifically, with regard to the SIP Plans, there are two fundamental conflicts:**
    a. **First, SIP plan participants offer competing products to those offered by the SIP, so there is a disincentive to for such participants to invest in the products offered by the SIP if they can generate more revenue from their own proprietary products. How would having broker dealer representation on the Operating Committee address this conflict and do you believe there is an inherent conflict?**
    b. **Second, SRO participants sell competing market data products that compete with that of the SIP's. Does Chair White believe that the proprietary products are superior to those offered by the SIP's? Broker dealers are required to provide competitive trading products to their clients and have duties to provide best execution. Because of this obligation, they have to purchase both the proprietary products and the products from the SIP. If the SIP products are of decreased quality or if there are latency issues, ultimately this means that investors would receive a lesser quality of information both in time and substance if they only received products from**

[45] The recommendations can be found at the EMSAC Spotlight Page. *See* Memorandum from the EMSAC Trading Venues Regulation Subcommittee to the Equity Market Structure Advisory Committee (Apr. 19, 2016), https://www.sec.gov/spotlight/emsac/emsac-trading-venues-subcommittee-recommendations-041916.pdf (Re: Recommendations Relating to Trading Venues Regulation).

the SIP. Can you please address these aforementioned concerns and address whether or not the SIP products are of lesser quality, and if investors only received data from the SIP, whether such investors would be at disadvantage and incur higher costs.

Response: As you note, the SROs provide consolidated market data jointly through the SIPs, and exchange SROs individually provide their own proprietary market data products. This has led some market participants to express concern that the exchange SROs may have incentive to underinvest in the consolidated market data product (*i.e.*, the SIPs) to make their proprietary market data relatively more attractive.

These concerns are understandable. The integrity and quality of the consolidated SIP market data feed, given its role as a benchmark pricing mechanism for investors, is of paramount importance. Following the August 2013 outage of the Nasdaq SIP, I stressed the need for the SROs improve the resilience and robustness of the SIPs such that the disaster recovery capabilities allow the SIPs to recover operations more quickly. Measures have now been put in place to provide a "warm" backup site within ten minutes. In addition, beginning last November, the SIPs because subject to the new technology standards for operational integrity set forth in Regulation SCI. [46]

The SROs also have taken steps, at my request, to improve the timeliness and transparency of the SIPs. The consolidated market data plans have steadily upgraded their systems to reduce average latencies from nearly one second a decade ago to less than 1/1000th of a second today.[47] The dissemination of SIP data will necessarily be slightly slower than proprietary market data, given that SIP data must go through the consolidation process, but, as noted above, we have worked with the SROs to steadily shorten that differential, and today, the delay is routinely less than one millisecond.[48] In addition, as requested, the SIPs have added a timestamp on the consolidated data feeds that reflects, for each order or execution processed by an exchange, the event processing timestamp that is reflected on the exchange proprietary data feed. This new time stamp is in addition to the timestamp showing the processing time at the SIP itself and allows market participants to more readily assess the absolute and relative latencies of each.

Finally, the Commission has taken enforcement action to ensure the timeliness and integrity of consolidated market data, as evidenced by its settled action against the NYSE for disseminating proprietary market data in advance of it being sent to the SIP.

[46] See New York Stock Exchange LLC and NYSE Euronext, Exchange Act Release No. 67857 (Sept. 14, 2012), https://www.sec.gov/litigation/admin/2012/34-67857.pdf.
[47] *See* Exchange Act Release No. 70010 (July 19, 2013), 78 Fed. Reg. 44984 (July 25, 2013) (CTA/CQ-2013-04), https://www.sec.gov/rules/sro/nms/2013/34-70010.pdf.
[48] For latency information on the CTA Plan, *see* CONSOLIDATED TAPE ASSOCIATION, KEY OPERATING METRICS OF TAPE A&B U.S. EQUITIES SIP, https://www.nyse.com/publicdocs/ctaplan/notifications/trader-update/CTA%20SIP%204Q15%20Consolidated%20Data%20Operating%20Metrics%20Report%20(Completed).pdf. For latency information on the UTP Plan, *see* UTP PLAN, UTP Q2 2016: U.S. EQUITIES UTP SIP KEY QUARTERLY OPERATING METRICS OF TAPE C, http://www.utpplan.com/DOC/UTP%202016-Q1%20Stats%20with%20Processor%20Stats.pdf.

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5. **Additionally, Chair White, can you provide specific commentary on the draft legislation that I have been working on with regard to reforming NMS governance and how this legislation would provide for increased transparency in the current NMS governance model? Do you believe that having broker dealer representation on the Operating Committees would be beneficial to the market as a whole, and do you believe this bill accomplishes that goal? If no, how would you change it so that it does achieve that goal?**

<u>**Response**</u>: As noted above, NMS plan governance is one of the many important topics the Commission currently is assessing as part of its broad-based review of equity market structure. Most recently, the EMSAC provided recommendations on this topic. I am carefully considering these recent EMSAC recommendations as I develop further my views on this issue.

6. **In your recent speech regarding offering reform, you claim that the SEC has "always periodically reviewed the operation of the major rules." Where is the evidence of these reviews? Might I ask, as a matter of course when the SEC has promulgated a new rule or amendment, has the SEC ever recently eliminated an outdated or duplicative rule?**

<u>**Response**</u>: The Commission and its staff have formal and informal processes for identifying existing rules for review and for conducting those reviews to assess the rules' continued utility and effectiveness in light of continuing evolution of the securities markets and changes in the securities laws and regulatory priorities. For example, in accordance with current statutory requirements, we conduct 10-year retrospective rule reviews under the Regulatory Flexibility Act ("RFA")[49] and Paperwork Reduction Act reviews of information collections. In addition to the annual list of rules scheduled for a 10-year review, the Commission also publishes twice yearly an agenda of anticipated rulemaking actions pursuant to section 602(a) of the RFA.[50] The agenda includes both potential changes to existing rules, including rescission, and new rulemaking actions. The SEC's most recent agenda includes a number of existing rules that are under consideration for revision and updating, including proposed rules to modernize and clarify the disclosure requirements for companies engaged in mining operations, proposed rules to update certain disclosure requirements in Regulations S-X and

[49] The RFA sets forth specific considerations that must be addressed in the review of each rule: (i) the continued need for the rule; (ii) the nature of complaints or comments received concerning the rule from the public; (iii) the complexity of the rule; (iv) the extent to which the rule overlaps, duplicates or conflicts with other federal rules, and, to the extent feasible, with state and local governmental rules; and (v) the length of time since the rule has been evaluated or the degree to which technology, economic conditions, or other factors have changed in the area affected by the rule. *See* 5 U.S.C. § 610(c). The most recent list of SEC rules to be reviewed pursuant to the RFA can be found at https://www.sec.gov/rules/other/2015/33-9965.pdf.

[50] The complete agenda is available at www.reginfo.gov, and information on regulatory matters in the agenda is available at www.regulations.gov.

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S-K, and proposed rules to modernize Rule 147 under the Securities Act of 1933 to facilitate intrastate and regional securities offerings.

In addition to these formal processes, the Commission and its staff frequently receive and consider suggestions to review existing rules through various types of communications, ranging from formal petitions for rulemaking to informal correspondence from investors, investor and industry groups, Congress, fellow regulators, the bar, and the public. Likewise, the Commission and staff frequently discuss the need to revisit existing rules through formal and informal public engagement, including advisory committees, roundtables, town hall meetings, speeches, conferences, and other meetings.

7. **Congress mandated that the SEC hold the annual forum on Small Business Capital Formation. The forum is no different than the creation by Congress of the Investor Advisory Committee. However, there are some commentators, activists and Members of this Committee that would dismiss the forum's recommendations. Do you agree that the forum's recommendations are not persuasive and should not receive the Commission's attention and action by the Division of Corporation Finance?**

Response: The recommendations of the Government-Business Forum on Small Business Capital Formation should, and do, receive the Commission's serious attention. The Forum's recommendations represent the views of the participants, who bring the experience of active market participants in small business capital formation.

The Commission has adopted reforms that were recommended by the Forum participants, or put forth by the Commission's Advisory Committee on Smaller Public Companies and endorsed by the Forum participants. These reforms include:

- simplifying the disclosure and reporting requirements for smaller companies and allowing smaller companies to provide scaled disclosures;
- amending Rule 144 to shorten the holding period requirement for the resale of restricted securities; and
- adopting a rule specifying that employee stock options issued in compensatory transactions not be considered a class of equity securities for purposes of triggering the registration requirements under Section 12(g) of the Securities Exchange Act of 1934.

8. **Now that the Commission has approved the major JOBS Act rulemakings, are there additional ideas that have been raised in the JOBS Act rulemaking comment periods that you believe would further enhance capital formation for small companies?**

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Response: The SEC is very interested in pursuing new ideas that would facilitate capital formation and reduce regulatory burdens, including for small businesses, while maintaining the necessary investor protections. For example, the Commission recently proposed amendments to existing Securities Act Rule 147 to modernize the rule for intrastate offerings to further facilitate capital formation, including through intrastate crowdfunding provisions. The proposal also would amend Securities Act Rule 504 to increase the aggregate amount of money that may be offered and sold pursuant to the rule from $1 million to $5 million and apply bad actor disqualifications to Rule 504 offerings to provide additional investor protection. These changes were proposed based on feedback that the SEC received while working on the final rules for crowdfunding under Title III of the JOBS Act.

In addition, the recently enacted FAST Act includes provisions designed to benefit smaller reporting companies, including forward incorporation by reference and disclosure reform. The Commission has adopted interim final rules regarding forward incorporation by reference, and staff is currently preparing recommendations to the Commission for implementation of disclosure reform.

9. **Should the SEC be regularly updating its rules to ensure that all companies can access the capital markets without having to comply with a one-size-fits-all compliance regime? I have seen little evidence that the Commission has moved to streamline or eliminate rules that are "outmoded, ineffective, insufficient, or excessively burdensome." How will the Commission address these retrospective reviews in FY 2016?**

Response: The SEC currently is engaged in broad-based reviews of Commission rules and regulations in a number of areas. For example, I recently instructed the staff to take a fresh look at the SEC's existing offering rules to develop ideas for the Commission to consider that would reduce the regulatory burdens on small business capital formation in a manner consistent with investor protection. One result of this review was the Commission's recent proposal to modernize Rule 147 under the Securities Act of 1933 to facilitate intrastate and regional securities offerings. In recognition of the transformative nature of the internet and other technologies, the rule would, among other things, eliminate the existing intrastate restriction on offers and ease some of the issuer eligibility requirements to make the rule available to a greater number of businesses seeking financing in-state.

In addition to such targeted reviews, as noted above, we conduct 10-year retrospective rule reviews under the Regulatory Flexibility Act on an annual basis.[51] The RFA requires agencies to review each final rule that has a significant economic impact upon a substantial number of small entities. The goal of the review is to "determine whether such rules should be continued without change, or should be amended or rescinded, consistent with the stated objectives of applicable statutes, to minimize any significant economic impact of the rules

[51] The most recent list of SEC rules to be reviewed pursuant to the RFA can be found at https://www.sec.gov/rules/other/2015/33-9965.pdf.

upon a substantial number of such small entities." The Commission also publishes twice yearly an agenda of anticipated rulemaking actions pursuant to section 602(a) of the RFA. The agenda includes both potential changes to existing rules, including rescission, and new rulemaking actions. I expect that in FY2016 and FY2017, the Commission will continue its current review processes, combining the mandatory 10-year reviews required by the RFA with targeted reviews prompted by market developments, industry and other public input, or other specific facts that give rise to a targeted review.

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Questions for the Record from
Rep. Blaine Luetkemeyer (MO-03)
Committee on Financial Services
U.S. House of Representatives

"Examining the SEC's Agenda, Operations, and FY 2017 Budget Request"

Hearing held on November 18, 2015

To Chair White:

1. **To what degree has the SEC coordinated with the Department of Labor (DOL) on the DOL fiduciary rule? Please provide specific evidence of coordination and cooperation.**

2. **Why has the SEC chosen to allow DOL to impose sweeping rules that will greatly impact investors and institutions that fall under your supervisory jurisdiction?**

3. **Does DOL possess the authority to change the definition of "investment advice"?**

4. **Has the SEC completed an economic analysis, formal or informal, of the proposed fiduciary rule? To your knowledge, has DOL completed an economic analysis of the proposed rule?**

Response: Consultation among the DOL and the Commission has been, and will continue to be, important. Commission staff provided technical assistance in connection with DOL's rule. Specifically, Commission staff met with staff from DOL on a number of occasions, providing technical expertise regarding the regulation of investment advisers and broker-dealers, including disclosure requirements and our approach to the conflicts that surround, among other things, principal trading, differential compensation, and receipt of commissions. I also discussed issues related to the rulemaking with Secretary Thomas Perez on the phone or in person on several occasions between late 2013 and early 2015, and with his predecessor on one occasion in mid-2013. In addition, on occasion, Commission staff economists discussed with DOL staff economists cost-benefit related issues as well as relevant academic literature. Finally, Commission staff provided technical comments on drafts in response to requests from staff from the Office of Management and Budget.

I recognize the concerns about consistency and the impact the DOL's rulemaking may have on Commission registrants, particularly broker-dealers. Of course, because the DOL has its own jurisdiction, statutes, and responsibilities, any rules the Commission adopts may or may not differ from DOL's final rule. As separate and distinct agencies, I believe that there is no reason why the SEC—if the Commission chooses to advance a proposal—and the DOL cannot each proceed independently. I also understand, however, the importance of consistency and considering the impact that potential fiduciary rulemaking by the SEC and the DOL may have on SEC registrants. Consultation among the two agencies has been, and will continue to be, important.

It is important to achieve the right balance in addressing these issues, while making sure investors, particularly retail investors, are appropriately protected and have access to the type of investment advice and services they need and can afford. I believe that ongoing analysis of potential impacts is required to achieve this balance and to identify possible costs. My goal and that of Commission staff is to continue to work together to coordinate all of our rules to the extent appropriate under our different statutory standards and mandates.

5. **The SEC has indicated interest in promulgating a separate fiduciary standard rule. Will you commit to conducting a thorough economic analysis of any SEC proposal on this matter?**

6. **Have you seen any evidence that there exists a systemic problem with the current fiduciary framework? Please provide the Committee with specific examples and details on the nature of this problem and the degree to which it exists in the current marketplace.**

Response: I have come to the conclusion that broker-dealers and investment advisers should be subject to a uniform fiduciary standard of conduct when providing personalized investment advice to retail investors. This is a complex issue, and, in proposing a uniform fiduciary standard, there are many questions that would need to be addressed, including how to define the standard with clear guidance on what it would require and how it would affect current business practices. SEC staff has provided a detailed outline to the Commission regarding a possible recommendation to impose a uniform fiduciary standard, and I have discussed my views with each of my fellow Commissioners. As part of its analysis, the staff is giving serious consideration to, among other things, the recommendations of a 2011 SEC staff study under section 913 of the Dodd-Frank Act, the views of investors and other interested market participants, potential economic and market impacts, and the information we received in response to the Commission's request for data.

Consideration of any potential rulemaking by the Commission will certainly take into account the potential impact on retail investors' access to affordable investment advice, and such a proposal would include a robust economic analysis. In addition, any Commission proposal would solicit public comments to better inform our efforts. I am committed to working with the Commission's economists in evaluating the costs and benefits of any potential approach so that we can further our goal of protecting investors without imposing unnecessary or unduly burdensome costs on them or the industry.

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Question for the Record of Cong. Luke Messer
Hearing of the House Financial Services Committee, November 18, 2015

Over the past decade, Congress and many agencies have focused considerable attention on reducing retirement plan costs. One proven avenue for driving down costs is through electronic delivery of the many notices, disclosures, and statements that retirement plans must distribute. Most rules governing electronic delivery of retirement plan materials are within the Labor and Treasury Departments' jurisdiction. But the delivery of prospectuses to retirement plan participants falls within the Commission's gambit.

As I understand, several retirement plan providers have been considering delivery of prospectuses and other materials required to be delivered under securities laws to plan participants such as immediate confirmations of plan transactions via e-mail to employees who participate in the provider's record kept retirement plans. The provider would rely on electronic delivery only if the employer (1) expressly agrees to that method of delivery and (2) provides email addresses for its employees for purposes of electronic delivery. It would seem that Example 1 in the Commission's 1996 Electronic Delivery Interpretive Release (Release No. 33-7288) makes this approach permissible for the various types of documents required under securities laws to be delivered to plan participants.

Madam Chairman, could you indicate whether your staff is examining this issue and, if so, when we might see confirmatory guidance?

Response: The Commission's staff has, in the past, provided informal advice that investment professionals hired by an employer, as well as the employer itself, could rely on Example 1 to administer that employer's employee benefit plans. The staff has indicated that an investment professional may deliver documents required to be delivered to that employer's employees through the employer's e-mail system to employees who use the employer's e-mail system in the course of performing their duties or who are expected to have alternative means made available to receive email messages. The staff is currently considering whether to issue additional guidance.

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Question for the Record of Congressman Ed Perlmutter (CO-7)
Hearing of the House Financial Services Committee, November 18, 2015

Over the past several years, Congress and many agencies have focused considerable attention on reducing retirement plan costs. One proven measure for driving down costs is through electronic delivery of the many notices, disclosures, and statements that retirement plans must distribute. Most rules governing electronic delivery of retirement plan materials are within the Labor and Treasury Departments' jurisdiction. But the delivery of prospectuses to retirement plan participants falls within the Securities and Exchange Commission's purview.

As I understand, several retirement plan providers have been considering delivery of prospectuses and other materials required to be delivered via email to plan participants such as immediate confirmations of plan transactions to employees who participate in the provider's record-kept retirement plans. The provider would rely on electronic delivery only if the employer (1) expressly agrees to allowing email delivery and (2) provides email addresses for its employees for purposes of electronic delivery. It seems Example 1 in the Commission's 1996 Electronic Delivery Interpretive Release (Release No. 33-7288) lays the groundwork for making this approach permissible for the various types of documents required under securities laws to be delivered to plan participants.

Chair White, I'm curious if your staff is examining this issue and, if so, when we might see guidance?

Response: The Commission's staff has, in the past, provided informal advice that investment professionals hired by an employer, as well as the employer itself, could rely on Example 1 to administer that employer's employee benefit plans. The staff has indicated that an investment professional may deliver documents required to be delivered to that employer's employees through the employer's e-mail system to employees who use the employer's e-mail system in the course of performing their duties or who are expected to have alternative means made available to receive e-mail messages. The staff is currently considering whether to issue additional guidance.

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QFR for SEC Chair White from Rep. Neugebauer:

Chair White, the Commission and its staff now accumulate a tremendous amount of proprietary information from firms it regulates. For example, you are gathering systemic risk filings, and many other types of highly sensitive information, like "orderly resolution plans" for asset managers.

Chair White, the firms you regulate are now required to protect this information from being misused or stolen, but what about the SEC itself?

Response: We recognize the importance of and are committed to protecting data provided by registrants and other parties as well as information originating from within the SEC. To this end, the SEC adheres to a framework based on guidance from the National Institute of Standards and Technology ("NIST") that focuses on implementing management, operational, and technical security controls within agency information systems and technologies. NIST requires the implementation of over 200 baseline security controls that are predicated on the security classification of data stored, processed, and transmitted by each SEC information system.

We continually assess the security posture of all SEC assets and associated security controls through the implementation of a robust Security Assessment and Authorization ("SA&A") process in accordance with Federal Information Processing Standards and NIST guidance. Included in our SA&A process are detailed security control reviews by independent assessors and intrusive penetration tests conducted by professionals in the field.

In addition, we have invested in advanced technical capabilities that enhance our ability to detect, react, and respond to network attacks and anomalies. The SEC has deployed many of these technologies and is continuously evaluating its portfolio to look for new tools and enhancements to augment our program. Our security devices, practices, and protocols detect and respond to attempted attacks every day.

In addition to following best practices for security devices, firewalls, and other protections, we emphasize that our first line of defense is our staff. Security Awareness and Training is conducted on a regular basis to teach and reinforce all employees and contractors how to protect information that could be considered sensitive, non-public, or personally identifiable information ("PII"). We believe that our annual security training is a valuable resource for staff and we plan to continue to invest in our security training and awareness programs.

Can you tell the committee about the internal controls you have placed upon yourselves to protect this information, such as cyber-attacks like OPM experience, or misuse by staff or former staff?

Response: The SEC has worked to address such threats using a multi-pronged strategy based on the NIST Cyber Security Framework. Perhaps the most critical aspects of the framework are those controls that protect information stored, processed, and transmitted by SEC information systems. Among the controls the SEC has implemented to protect data from misuse and compromise are:

- Encryption of information both in transit and at rest. SEC physical assets (such as laptops and mobile devices) are encrypted, which secures information while at rest.

- Use of secure email protocols to better ensure the security of information that could be considered sensitive, non-public, or may implicate PII.

- Implementation of two-factor authentication, an authentication model which requires users to possess multiple user identifiers for remote access to the SEC network.

- Development and execution of a security-focused software development model to ensure that security requirements are incorporated and security controls are implemented into core SEC information systems and applications that store information from registrants and other associated stakeholders.

- Advancement of our 24x7x365 Security Operations Center which is responsible for monitoring, assessing, and responding to potential network anomalies and confirmed attacks on the SEC environment.

- Enhancement of our training programs. All employees must take an annual security awareness course and certain employees, such as the exam staff, participate in additional training about securing information specific to their job duties.

We are confident in our approach to managing cyber security risk and threats to the SEC's operating environment, but we are constantly looking for ways to enhance the security of our systems.

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Representative Bruce Poliquin (ME-2)
Questions for the Record
"Examining the SEC's Agenda, Operations and Budget Request for FY 2017"
November 18, 2015

1.) Chair White, Secretary Perez has testified that the Department of Labor has consulted with the SEC in the developing their proposed fiduciary standard. Can you please elaborate on the specific ways those consultations occurred between the SEC and the Department of Labor?

2.) Did anyone at the SEC provide written comments or feedback to the Department of Labor on the Fiduciary Rule? If so, can you please provide the Committee with these written comments?

3.) Did anyone on the SEC staff [informally] verbally advise or consult with, or provide verbal comments to, Department of Labor regarding the proposed rule? If so, can you please provide the Committee with any emails or other correspondence prepared in connection with the SEC's verbal communications regarding the Department of Labor's rulemaking process?

Response: Consultation among the DOL and Commission staff has been, and will continue to be, important. Commission staff has also provided technical assistance in connection with DOL's rule. Specifically, from the period beginning in mid-2013, Commission staff met with staff from DOL on a number of occasions, providing technical expertise regarding the regulation of investment advisers and broker-dealers, including disclosure requirements and our approach to the conflicts that surround, among other things, principal trading, differential compensation, and receipt of commissions. I also met with Secretary Thomas Perez in person several times between late 2013 and early 2015 and we have spoken over the phone about the DOL's fiduciary rulemaking, and I met with his predecessor on one occasion in mid-2013. In addition, on occasion Commission staff economists discussed with DOL staff economists cost-benefit related issues as well as relevant academic literature. Finally, Commission staff provided technical comments on drafts in response to requests from staff from the Office of Management and Budget.

Your question also requests that the Commission produce certain inter-agency communications regarding the pending DOL rulemaking proposal. Pursuant to the December 18, 2015 request letter signed by Subcommittee Chairman Garrett, the staff sent a copy of the document production provided to the U.S. Senate Committee on Homeland Security and Governmental Affairs to the House Financial Services Committee on January 8, 2016. This production contained inter-agency communications responsive to your requests.

4.) A bipartisan group of Committee members have introduced legislation to create the Office of Small Business Capital Formation, on par with the SEC's Investor Advocate. Do

you support this proposal? How would it be helpful to the SEC's capital formation agenda?

Response: Facilitating capital formation is one of the three tenets of the SEC's mission and our work in this area continues to focus on ways to improve access to capital, with a particular emphasis on small businesses. In carrying out our mission, we seek to ensure that the views of small business owners, investors, and other stakeholders in the small and emerging business community are clearly heard.

The Commission has an Office of Small Business Policy within the Division of Corporation Finance that maintains a sharp focus on capital formation for small businesses. This office:

- Responds to over 1,000 small business-related inquiries every year—the staff speaks directly to anyone who calls or emails requesting interpretive guidance;
- Provides interpretive guidance on the SEC's website and participates in SEC rulemaking and other actions that affect small businesses;
- Provides support to the Commission's Advisory Committee on Small and Emerging Companies;
- Coordinates the Commission's Annual Government-Business Forum on Small Business Capital Formation; and
- Acts a liaison to the state securities regulators and the Small Business Administration on corporate finance issues that impact small business.

While I fully appreciate that objective of a new Office of Small Business Capital Formation, I do have concerns about duplicating or disrupting offices and programs that already exist, which could lead to fragmentation of small business considerations within the agency and additional organizational complexity. For example, depending on the statutory role that such an advocate would be given in policymaking and rulemaking initiatives, it could add an additional layer of complexity to our internal processes for providing interpretive guidance and issuing rules.

5.) Can you identify any "low hanging fruit" in terms of clearly outdated, duplicative, unnecessary, or overly burdensome disclosure requirements that can be amended or eliminated in the near term while the staff engages in a more comprehensive review of the SEC's corporate disclosure system?

Response: As part of the Disclosure Effectiveness initiative, in July 2016 the Commission proposed to amend certain of its disclosure requirements that may have become redundant, duplicative, overlapping, outdated, or superseded, in light of other Commission disclosure requirements, U.S. Generally Accepted Accounting Principles ("U.S. GAAP"), International Financial Reporting Standards ("IFRS"), or changes in the information environment. The Commission also solicited comment on certain Commission disclosure requirements that overlap with, but require information incremental to, U.S. GAAP to determine whether to retain, modify, eliminate, or refer them to the Financial Accounting Standards Board

("FASB") for potential incorporation into U.S. GAAP. The proposals are intended to facilitate the disclosure of information to investors, while simplifying compliance efforts, without significantly altering the total mix of information provided to investors.

This release contains four categories of proposed revisions:

1. Redundant or Duplicative: We have proposed to eliminate Commission disclosure requirements that require substantially the same disclosures as U.S. GAAP, IFRS, or other Commission disclosure requirements. For example, Rule 10-01(b)(2) of Regulation S-X requires the presentation of earnings per share on interim income statements. FASB Accounting Standards Codification 270-10-50-1(b) also requires this presentation. We propose to delete the requirement in Rule 10-01(b)(2) to present earnings per share.

2. Overlapping: These are Commission disclosure requirements that are related to, but not the same as, U.S. GAAP, IFRS, or other Commission disclosure requirements. We propose deleting overlapping disclosure requirements that either: (1) require disclosures that convey reasonably similar information to or are encompassed by the disclosures that result from compliance with the overlapping U.S. GAAP, IFRS, or Commission disclosure requirements, or (2) require disclosures incremental to the overlapping U.S. GAAP, IFRS, or Commission disclosure requirements and may no longer be useful to investors. Where Commission disclosure requirements overlap with, or require information incremental to, other Commission disclosure requirements, we propose to integrate the requirements.

   For example, Regulation S-X identifies for disclosure three assumptions related to insurance liabilities stated at present value. U.S. GAAP, however, does not limit its disclosures to these three assumptions but, rather, provides additional examples of assumptions. Accordingly, we propose to delete the overlapping disclosure requirements in Regulation S-X.

   Where Commission disclosure requirements overlap with U.S. GAAP but require information incremental to U.S. GAAP, we solicit comment on whether to retain, modify, eliminate, or refer them to the FASB for potential incorporation into U.S. GAAP.

3. Outdated: We propose to eliminate Commission disclosure requirements that have become obsolete as a result of the passage of time or changes in the regulatory, business, or technological environment. For example, various Commission disclosure requirements and forms require issuers to disclose the availability of their filings for reading or copying at the Commission's Public Reference Room. Generally, issuers are required to file most filings electronically, and, with the widespread availability of the Internet, investors can access for free substantially all issuers' Commission filings on EDGAR. We propose to delete the requirements to identify the Public Reference Room and disclose its physical address and phone number. Instead, filings would

disclose the Commission's Internet address and that electronic SEC filings are available there.

4. Superseded: We propose to update disclosure requirements that have been superseded by recent legislation, more recently updated Commission disclosure requirements, or more recently updated U.S. GAAP requirements. For example, there are references in our rules to "pooling-of-interest accounting" and "extraordinary items," which are no longer part of GAAP. To update Commission disclosure requirements, we propose to delete these references in our rules and forms.

The proposals are also part of the Commission's efforts to implement Title LXXII, Section 72002(2) of the Fixing America's Surface Transportation Act, which, among other things, requires the Commission to eliminate provisions of Regulation S-K that are duplicative, overlapping, outdated, or unnecessary.

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November 18, 2015

Member: Rep. Scott Tipton

Question for Witness: SEC Chair Mary Jo White

Question:

- **Chair White, I understand that the SEC is currently working to review and update certain industry guides, specifically Industry Guide 7 (IG7), which contains the SEC's basic disclosure policy for mining companies. As the mining and minerals industry becomes increasingly globalized, it is apparent that the reporting disparities between U.S and foreign jurisdictions are having a negative impact on U.S. companies who operate in multiple jurisdictions and burdens them with a competitive disadvantage, impeding their ability to create jobs and spur economic growth. Please tell me where efforts to update IG7 are at in the process and when we can expect it to be completed?**

Response: On June 16, 2016, the Commission proposed rules to modernize the disclosure requirements for mining properties by aligning them with current industry and global regulatory practices and standards. If adopted, the proposed rules would rescind Industry Guide 7. The proposed rules were subject to a comment period, which closed on September 26, 2016. The staff will carefully consider the comments received in developing recommendations for a final rule for the Commission's consideration. Although it is impossible to predict when the Commission might complete a rulemaking, it is important that it be advanced as soon as possible.

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Rep. Royce

In reviewing a recent report by the LEI Regulatory Oversight Committee (attached), I noticed that of the 8 SEC rules, or proposed rules, listed in the report, that the LEI is required in only one case. In all other cases, the LEI is only requested. Given the importance the LEI will play in enhancing better systemic risk management, I would appreciate if you could review the list, and let me know why the SEC is not taking stronger steps to ensure adoption. Information would also be useful on how the SEC plans to incorporate the LEI in future rulemakings.

Response: As I stated during the hearing, I believe that the LEI is an important tool that can enable regulators to link participants in financial markets to their activities and to the risk exposures those activities create.

Indeed, the SEC has been a strong participant in the global efforts to establish and implement the LEI. The Commission has incorporated the LEI into rulemakings to facilitate data analysis across regulatory filings. For example, in the recent SBSR rulemaking, the Commission incorporated the use of LEIs to identify counterparties to security-based swaps and mandated that participants at registered SDRs obtain an LEI. I believe that the presence of LEIs in security-based swap data made available to the Commission will enhance the Commission's ability to monitor this market for abuse and to identify build-ups of credit and counterparty risk that could form as a result of transaction activity.

More generally, as we contemplate future rulemakings, we will continue to consider the appropriate use of LEIs. For example, rules that require financial market participants to furnish the Commission or the public with information about themselves or about their activities, similar to those adopted in the security-based swap market, will be candidates for the Commission to consider inclusion of LEIs.

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Response to questions from Rep. Wagner concerning DOL fiduciary rulemaking

NOTE: *During Chair White's testimony before the Committee on Financial Services of the U.S. House of Representatives, Representative Wagner requested that Chair White follow up with responses to particular questions. The relevant portion from the hearing transcript is excerpted below, and Chair White's response follows.*

Transcript Excerpt
WAGNER:
In following up on some of the questions that have been asked about the DOL fiduciary rulemaking, I do want to associate myself with my friend, the gentleman from Georgia, Mr. Scott.

WAGNER:
In the SEC's absolutes purview on anything having to do with the uniform fiduciary rule.
And following up on what the chairman said, you talked about, last -- the last SIFMA annual meeting, about this full out focus.
So what does full out mean to you? When can we expect a rulemaking?

WHITE:
I mean again, I want to make clear at the outset, this is my view; it will be ultimately a commission decision. I have obviously given staff direction, and they're very, very actively working on it. It's complex, it's not quick, but we're working toward -- you know, in the very short-term the -- most of the details of what the proposal would be.
Now that doesn't suggest in two months, you're going to see a proposal. This is a long, complex exercise, and it has to involve the full commission.

WAGNER:
It does, and I'm glad to see that you're looking at a shorter-term rather than the longer-term, and obviously, you'll need to come back before this committee and Senate banking; you have to talk about alternative remedies to a uniform fiduciary standard that would address investor confusion, including simplifying of titles, and enhancing disclosure.
All of these things are things that I hope are part of this ongoing analysis.

David Grim, with your division of investment management stated that further analysis still had to be done. What the scope of analysis, and what do you anticipate is the timeline for completing it?

WHITE:
Again, I cannot, you know, kind of overstate the complexity and the importance of getting this right, and part of that is clearly the very deep economic analysis that our economists will do as we are proceeding with that. So, in terms of impacts, in terms of -- you know, for example, I think have said this before, I mean, if we ended up at the end of the day with a rule imposed that uniform fiduciary duty, but we deprived retail investors of reliable, reasonably priced advice, you know, we would not have succeeded, obviously.
And so, our economists have a lot of work to do as we proceed with this.

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WAGNER:
Well, and you're right, we have to get right, and I think the DOL proposal is a 1,000 pages wrong.
So, can you -- tell us about, in your analysis, including in a study of the impact of the DOL's proposed rule on investment advisers registered with the SEC?

WHITE:
You know, I mean, I think -- I mean, it would have impact, I think, on investment advisers as well as broker-dealers. I mean, what we did with the DOL proposal, though, was essentially, as I mentioned before, provided technical assistance to them, which included -- from our staff and it's our staff, you know, are providing how it might impact on investors and how it might, you know, what -- what the lay of the land is now in terms of how brokers operate, how investment advisers operate.
I mean, it really depends on -- and obviously, the Department of Labor is taking in a lot of comments about impacts. And so it depends on, you how, that...

WAGNER:
Tens of thousands of comments. And in fact, we received a letter, I received a letter from Secretary Perez, stating that they were going to make no changes, no re-proposals, even prior to the public comment period opening up.

And I am very dissatisfied with this. I know you said that you're taking technical -- are providing technical assistance, and in that quote before Senate Banking, you even talked about, particularly the lower end, which I care deeply about, in terms of customers' choice, access to products, cost of those products. I think that is absolutely key.
Do you have any concerns that some U.S. investors could potentially suffer based on the new fiduciary definition that the DOL is proposing?

WHITE:
Well, you know, I don't want to comment on that specifically, other than to say that I think the Department of Labor is -- and certainly, you know, our technical assistance was included, you know, that concern as you perceive with any rulemaking, and we have it in proceeding with ours.

WAGNER:
Well, I'm just looking at a couple examples, here, on how the DOL -- I think, conflicts with securities laws. And -- and I understand that DOL's fiduciary duty rule will require financial advisers to provide 1, 5, and 10 year projections on investment returns as part of projecting investment costs under the best interest contract exemption.
Does this potentially conflict with the Investment Advisers Act of 1940, especially its antifraud provisions?

WHITE:
Well, I mean, I think -- I'd have to analyze that with the -- my folks in the invest management division, specifically. But -- but what I indicated earlier is even now we have different roles in

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the ERISA space -- it's different statutory authority that apply to our brokers, our registrants than the federal securities laws require. But I'm happy to get back on a specific one.

WAGNER:
I -- I'd like that -- for you to take a look at that, and also just -- just with the indulgence of the chairman.

Take a look the DOL (sic) definition and term on -- on recommendation. It differs completely from the definition used by FINRA. So I am concerned about some of these differences and -- and really reiterate this is the FTC's purview through 913, and we would love you to move as quickly as possible.

Thank you Mr. Chairman.

Response: You asked whether the requirement in the Department of Labor ("DOL") proposed fiduciary rule that registered investment advisers provide 1, 5, and 10 year projections on investment returns conflicts with the federal securities laws and the Investment Advisers Act of 1940 ("Advisers Act") in particular. The Advisers Act and related rules do not include such a requirement. I note that the DOL's final version of the Best Interest Contract Exemption eliminated that proposed requirement, and thus the exemption does not differ from the federal securities laws in this way.

You also asked about the DOL's definition of "recommendation," noting your view that it conflicted with FINRA's definition of "recommendation." I note that the DOL stated in its final rule defining who is a "fiduciary" under ERISA and the Internal Revenue Service Code that it "has taken an approach to defining 'recommendation' that is consistent with and based upon FINRA's approach," and that its definition of "recommendation" in the final rule, for example, "mirrors" and "conforms to" FINRA guidance on whether a communication will be viewed as a recommendation.[52]

I appreciate the concerns about the interplay between the DOL's new rule and requirements under the federal securities laws and FINRA's rules, and the application of different standards to the provision of investment advice to retail investors. I also understand the importance of consultation among the agencies (including self-regulatory organizations like FINRA, which DOL also consulted in connection with its rulemaking), and I appreciate the impact the standards established in DOL's new rule and related exemptions may have on regulated entities, investors, and the markets. However, since DOL just adopted its new rule at the beginning of April, and compliance with the rule is not required until next year, it is too early to determine the rule's impact. We will continue to coordinate with DOL regarding any issues or conflicts that may arise as the DOL rule is implemented.

[52] Definition of the Term "Fiduciary"; Conflict of Interest Rule—Retirement Investment Advice, 81 Fed. Reg. 20946, 20972 (Apr. 8, 2016), https://webapps.dol.gov/federalregister/PdfDisplay.aspx?DocId=28806.