OVERSIGHT OF THE SEC'S AGENDA, OPERATIONS, AND FY 2014 BUDGET REQUEST

HEARING

BEFORE THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

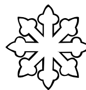
ONE HUNDRED THIRTEENTH CONGRESS

FIRST SESSION

MAY 16, 2013

Printed for the use of the Committee on Financial Services

Serial No. 113–20



U.S. GOVERNMENT PRINTING OFFICE

81–755 PDF WASHINGTON : 2013

For sale by the Superintendent of Documents, U.S. Government Printing Office
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CONTENTS

Page

Hearing held on:
May 16, 2013 1
Appendix:
May 16, 2013 53

WITNESSES

THURSDAY, MAY 16, 2013

White, Hon. Mary Jo, Chairman, U.S. Securities and Exchange Commission .. 8

APPENDIX

Prepared statements:
Neugebauer, Hon. Randy 54
White, Hon. Mary Jo 55

ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

Bachus, Hon. Spencer:
Letter to Federal Reserve Chairman Ben Bernanke dated March 14, 2013 79
Witness bio of Hon. Mary Jo White 81
Maloney, Hon. Carolyn:
Letter to Senator Jack Reed from SEC Chairman Mary Schapiro, dated November 28, 2011 82
Pearce, Hon. Stevan:
Article entitled, "Wind farms get pass on bald eagle deaths," dated May 14, 2013 86
Wall Street Journal article entitled, "SEC Bears Down on Fracking," dated August 25, 2011 92
White, Hon. Mary Jo:
Written responses to questions submitted by Representative Huizenga 95
Written responses to questions submitted by Representative McCarthy 98
Written responses to questions submitted by Representative Murphy 100
Written responses to questions submitted by Representative Pearce 101
Written responses to questions submitted by Representative Stivers 103
Additional information provided for the record in response to questions posed by Chairman Hensarling and Representative Hultgren during the hearing 110

OVERSIGHT OF THE SEC'S AGENDA, OPERATIONS, AND FY 2014 BUDGET REQUEST

Thursday, May 16, 2013

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

The committee met, pursuant to notice, at 10:05 a.m., in room 2128, Rayburn House Office Building, Hon. Jeb Hensarling [chairman of the committee] presiding.

Members present: Representatives Hensarling, Miller, Bachus, Royce, Garrett, Neugebauer, McHenry, Pearce, Posey, Fitzpatrick, Westmoreland, Luetkemeyer, Huizenga, Hurt, Stivers, Fincher, Stutzman, Mulvaney, Hultgren, Ross, Pittenger, Barr, Cotton, Rothfus; Waters, Maloney, Velazquez, Watt, Sherman, Meeks, Scott, Green, Cleaver, Moore, Perlmutter, Himes, Peters, Carney, Sewell, Foster, Murphy, Delaney, Sinema, Beatty, and Heck.

Chairman HENSARLING. The committee will come to order. Without objection, the Chair is authorized to declare a recess of the committee at any time.

The Chair will now recognize himself for 4 minutes for an opening statement.

Like most Americans, I was both angered and appalled to learn of the IRS' campaign to selectively intimidate Americans based upon their political beliefs. And yet, it was just days ago that our President urged college graduates not to view the government as "some separate, sinister entity." And to ignore the voices warning that, "Tyranny is always lurking just around the corner."

But it is under this President's watch that we get the news that the IRS, perhaps the single most feared government agency, has been caught trampling upon our most sacred right, namely our freedom of speech. Using the IRS to selectively punish and harass one's political opponents is right out of the Watergate playbook, a playbook I thought had disappeared 40 years ago. In 2013, this is something that we would expect perhaps in Venezuela or Cuba, but not in the United States of America.

This is an issue that should rise above partisanship. It hits at the heart of who we are as a people, and why we fight for justice and fear such a large powerful government that clearly has become too big to manage.

What the IRS did was wrong, because it tried to turn our citizens into subjects. It is wrong because it violates both our constitutional and civil rights. It is wrong because it treats citizens wishing to

speak out against the government's policies, exercising a God-given right, like enemies under state investigation.

In a word, Mr. President, it is tyranny. Now fearful and outraged Americans want to know just how pervasive the IRS' tactics of harassment have become within the Administration.

So, the question is most relevant to this SEC oversight hearing we are having today. The SEC has three statutory purposes: protecting investors; maintaining fair, orderly, and efficient markets; and facilitating capital formation.

And that is why it is most disturbing to many of us to realize that while the SEC has missed numerous mandatory rulemaking deadlines, it is devoting time and resources to a discretionary rulemaking, and more specifically, a highly controversial discretionary rule to force public companies to report all perceived facets of political involvement.

This rulemaking is well known to be a part of a partisan political agenda of labor union bosses, George Soros, and assorted leftist groups who conveniently would not have to abide by the rule.

Media Matters was quoted as saying that this is in part to "make the case that political spending is not within the fiduciary interests of publicly traded corporations and therefore, should be limited."

A New York City public advocate was quoted as saying, "Strength that all of these organizations can bring to bear against companies: boycotts; shareholder actions; legal actions; you name it, it is on the table."

The Center for Public Accountability: "We and our partners are putting pressure on companies to adopt political disclosure, to change the behavior of companies and trade associations and their political spending."

Now, the American people are horrified at those who would use the strong arm of government for partisan political advantage, but it remains to be seen whether this could ever happen at the SEC.

One of our chief oversight responsibilities regarding the SEC is to ensure the agency is a good steward of its resources, both its time and its budget, which has tripled over the last 10 years, and there are serious concerns.

These discretionary projects come at the expense of more important and legally required tasks that actually help struggling working families secure their financial futures, such as the bipartisan JOBS Act, which the SEC has regrettably and deliberately failed to implement on time.

A change in leadership represents an opportunity for a fresh start. While the SEC's recent history is riddled with misplaced priorities and misallocated resources, hopefully a fresh start is exactly what will happen at the SEC under the new leadership of our witness, Chairman White.

I now recognize the ranking member for 5 minutes for her opening statement.

Ms. WATERS. Thank you very much.

The Honorable Ms. White, I welcome you to the committee this morning. I congratulate you on your appointment and I am poised, as many of us are, to work with you to make sure the SEC can do its job.

And as you perhaps already know, it is not going to be easy. It is going to be very difficult for a lot of reasons. First, allow me to do everything that I can to make you feel comfortable in being here with us today, and while my colleague has referred to the debacle at the IRS, I assure you none of us think you had anything to do with that.

And so, you should not have to take any kind of reprimand. You should not have to endure any kind of similar criticism, and so I wish to say that on behalf of many of our colleagues who understand that you have this huge responsibility of being the cop on the block, I am focused at this particular time on something called cost/benefit analysis, and I am very worried.

I am very worried, and at question time, I will perhaps have the opportunity to raise some questions and create some discussion about cost/benefit analysis. The reason I am so focused on it is, I worked with institutional investors who came to us during the Dodd-Frank conference committee because they were concerned that many of the big companies that they were investing in appeared not to be under the control of a board of directors.

Many of them were not participating, and we still have questions that are going on in some of our big financial institutions about not only pay and other kinds of things, but whether or not some people should hold dual positions, as perhaps you are very much aware.

They came to us and they wanted to create an opportunity for our proxy materials to include the ability to nominate directors to those boards. They thought it was very important because, don't forget, they are the ones responsible for the retirements of our teachers, our firefighters, our police officers, and our first responders, all of those upon whom we depend.

And so, they want to have a say. They want to be involved. They want to be able to nominate and, lo and behold, some of my friends on the opposite side of the aisle teamed up with some of the business interests and went to court, into the 9th Circuit here in Washington, D.C., and they got a ruling against the SEC.

But the SEC went back and not only did they send out a directive to all of its personnel about, okay, let us see if we can do even better. They have a reputation for having done well on cost/benefit analysis.

And when we look at GAO, a report that took a look at how the SEC does cost/benefit analysis, they received compliments that they do a good job, but the court ruled.

The SEC has made an attempt to improve even more, but, lo and behold, we have a bill before us that is going to be on the Floor tomorrow, where the SEC is going to be challenged with the kind of burdens that are going to make your job even tougher, and there is no more money to go along with it.

And in addition to piling up unreasonable conditions on cost/benefit analysis, they are saying you must review it every 5 years, and you must go all the way back to the Depression era.

This is unreasonable, and I want you to know that while all this other stuff is going on, we still depend on you and the SEC, but you are going to be doing it with your hands tied behind you.

Because my friends who can rail about all of the other stuff that is going on—that makes for good propaganda—are not going to do

anything to help you get the resources you need to do your job. But some of us are committed to the proposition that if we are to protect investors, if you are to carry out your mission, that you must have the support, and we are going to fight for you.

We are going to fight for you, and we are not going to blame you for anybody else's mistake. You start anew in this job. You need to have the opportunity to get this job done.

Mr. Chairman, I yield back the balance of my time if I have any.

Chairman HENSARLING. The Chair now recognizes the chairman of the Capital Markets Subcommittee, the gentleman from New Jersey, Mr. Garrett, for 3 minutes.

Mr. GARRETT. I thank the chairman for holding this important hearing today, and I thank Chairman White as well for your participation.

Chairman White, I want to commend you, first of all, for your first month on the job. As indicated already, the job is only going to get only harder as the days go along.

It appears from what I have seen thus far, you are taking a pragmatic, commonsense approach to your issues at task, and I greatly appreciate it. I think this is refreshing.

But as you move forward, as has already been indicated, there will be pressures from outside forces that will begin to push you harder and more frequently.

And I encourage you to resist the temptation to take those more ideological, political positions, but continue as you have to seek logical, consensus-driven ones.

Your work and comments on Title VII, which is a cross-border application section, the JOBS Act implementation, the equity market structure prioritization, have all been very positive in my view.

So, I encourage you to continue down this pragmatic path, a reasonable path, and not be overly influenced by outside special interest and political groups.

And this brings me to the topic I am sure you have already heard about and will hear about today, as the chairman mentioned, our concerns are about an independent agency being subject to political pressure by the White House and this Administration and by outside political special interests groups.

There appears to be a coordinated effort to use any and all methods possible to tamp down political opposition, in some cases to stifle Americans' constitutional rights of freedom of speech.

This recent incident that had come to light just recently with the IRS has only helped crystallize for Americans exactly what this Administration and outside special interests appear to try to do.

Whether it is in the tax code, the corporate political disclosure process, union rules, EPA guidelines, et cetera, it becomes painstakingly clear that this Administration is more worried about crushing its political opposition than about governing and leading the American people through our current economic downturn.

Now I know, as indicated, you just started and you have not had anything to do with the issues as of yet. But we are just giving you an opportunity today to make a clear and emphatic statement that you will refuse to be bullied by these outside radical groups that are trying to exploit the corporate disclosure process.

Moreover, you are going to have an opportunity to make a clear and concise statement that you agree to formally and permanently remove the corporate political disclosure measure from your regulatory flexibility agenda.

As you are aware, these types of political witch hunts will only poison the well and make achieving your other priorities more difficult.

With all the important work the SEC has to do with finalizing the JOBS Act and Dodd-Frank rulemakings to policing bad actors in the market and working with Congress to reform the equity markets, it would be a shame to have these worthwhile goals suffer because of political and ideological pressure.

I think we should all agree that the SEC should remain focused on its core mission: protecting investors; ensuring orderly and fair markets; and facilitating capital formation—not on partisan political moves outside of your main purview that would limit the debate and deprive Americans of their constitutional rights.

Thank you, Mr. Chairman.

Chairman HENSARLING. The Chair now recognizes the gentlelady from New York, the ranking member of the Capital Markets Subcommittee, and notes her presence on the top row yet again. We are happy to have you rejoin us.

Mrs. MALONEY. Thank you.

Chairman HENSARLING. The gentlelady is recognized for 3 minutes.

Mrs. MALONEY. Three minutes, good heavens. First of all, thank you, Chairman Hensarling and Ranking Member Waters. And I would like to give an especially warm welcome to my fellow New Yorker, Chairman Mary Jo White.

I was absolutely so pleased when President Obama nominated you and even happier when you were confirmed by the Senate with such a strong bipartisan vote.

And I can say, from very close personal observation over her entire career, she will not be bullied. She has a career of great distinction in both the public and private sector.

I will never forget her touring the infamous Kenmore Hotel, probably the largest drug den in the City of New York, probably in the Nation, and it was the largest, I believe, public forfeiture where the Federal Government seized the property to stop the injustice of illegal drug dealing.

I want to report to her that it is now a very important community center serving people and helping people. That is just one example of her hands-on work on the ground.

She has taken on big issues, small issues, and has always been accessible. So, congratulations. My friend, Mel Watt, wants to know how you got confirmed so strongly. We would like to follow the same procedure and get him confirmed very quickly, too.

I am still deeply concerned over the fact that this country lost over $14 trillion in wealth in a financial crisis that economists tell us could have been prevented with stronger and better financial regulation.

So the country is looking to you for that leadership and I certainly will join with the ranking member and any likeminded member on either side of the aisle to work for you to get the resources

that you need in a position that has really grown in responsibility as your budget has decreased.

As you yourself have said, "The SEC has a number of new regulatory responsibilities, but because of sequestration we are unable to build the structure for that oversight that we are mandated to carry out."

It is our responsibility to give you those resources. There is a saying in New York that investors lost more in Madoff, in that scandal, than the SEC's entire budget since the Commission's inception in 1934.

So there is something seriously wrong with that. We just had a hearing last week on a number of derivatives bills that will be your responsibility to implement and to enforce.

And I look forward to working to make sure that you get your resources and that bills that are put in the area that I believe will create barriers to the SEC with your ability to get done, such as one that will be on the Floor tomorrow, we will be working together to help you get the resources you need.

I am so pleased with your appointment. Thank you for being here today. We look forward to your testimony.

Chairman HENSARLING. The Chair now recognizes the gentleman from Texas, Mr. Neugebauer, for 1 minute.

Mr. NEUGEBAUER. Thank you, Mr. Chairman, for holding this hearing.

And, Chairman White, welcome. Congratulations on your appointment.

I was just listening to my colleague on the other side of the aisle; that is a familiar story in Washington, "Well, we didn't do our job because we didn't have enough money." But when you go back and you look at the record, whether it is Madoff, Stanford, Bear Stearns, Lehman, or the Reserve Primary Fund, it wasn't necessarily a case that we didn't have regulations. It was a case that we had regulators who weren't actually doing their job.

And you go back and look at the record where the regulators had some reason to believe that Mr. Madoff was involved in some activities, but failed to follow up on it, and the same with Stanford.

So what we did is, since we had people who weren't doing their jobs, we went out there and said, let us pass some more regulations. That will help.

And so we went out and passed more regulations and now we have created this huge new risk category called regulatory risk that is impeding the ability of many of our financial institutions in America to be competitive.

And so, Chairman White, I hope that as you look at your organization, you are not necessarily looking for more resources, but making sure that the people under your charge are actually doing their jobs.

With that, I yield back my time.

Chairman HENSARLING. The Chair now recognizes the gentleman from Illinois, Mr. Foster, for 2 minutes.

Mr. FOSTER. Thank you. I thank the chairman and the ranking member.

Chairman White, I appreciate your testifying before our committee today, and I congratulate you on your nomination.

I want to emphasize to my colleagues the importance of fully funding the SEC. The President's request for Fiscal Year 2014 seeks $1.67 billion, a 26 percent increase in the current level, which is not incommensurate with your additional responsibilities in the wake of the financial crisis.

Some of my colleagues will assert that it is too costly to fully fund an agency whose primary responsibility is the regulation of the securities markets and a wide variety of other market issues, but I would respond by reminding my colleagues of the costs of deregulation and of inadequately funded regulators.

Families in America lost more than $16 trillion during the financial crisis of 2008, $16 trillion. That is, incidentally, or interestingly, enough to fully fund the SEC for about 1,000 years. Bearing in mind how many of our constituents lost their homes, retirement funds, and small businesses a short time ago, it is imperative that this Congress provide the agencies that are charged with policing the financial markets with the funding that they need to hire staff in the numbers and quality necessary to successfully execute their important tasks.

Thank you, and I yield back.

Chairman HENSARLING. The Chair now recognizes the gentleman from North Carolina, Mr. McHenry, for 1 minute.

Mr. MCHENRY. Chairman White, thank you so much for your leadership. I congratulate you on being the 31st Chair of the SEC.

Knowing tough prosecutions, such as the John Gotti case that you previously oversaw, I think Washington should be a little bit easier on you than that. Having said that—yes, exactly—having said that, we understand your commitment to the mission of the Securities and Exchange Commission, but we want to make it clear that we have statutory and legislative directives for the Securities and Exchange Commission to get on with the job of implementing the JOBS Act.

This is going to be a question that is going to be recurring, so the faster you get done with that, the more efficiently you get done with that, the better off we all are and we can move on to other questions.

With that, yesterday the House overwhelmingly passed a renewed Regulation A, giving the SEC a deadline for writing those regulations. I hope you will be able to comply with that statutory deadline. I welcome you for your first House testimony and I look forward to the answers to our questions.

Chairman HENSARLING. The Chair now yields 1 minute to the gentleman from Virginia, the vice chairman of the Capital Markets Subcommittee, Mr. Hurt.

Mr. HURT. Thank you, Mr. Chairman. And thank you for holding today's committee hearing. I, too, join in welcoming Chairman White to this committee.

I believe that the formal responsibility of this committee is to provide appropriate oversight and scrutiny of the Federal agencies' budgets under our jurisdiction. At a time when our Nation is approaching a national debt of $17 trillion, Federal agencies must learn to work smarter and to do more with less.

As we have seen from this budget request, the SEC has requested a 30 percent increase in funding. Undoubtedly, Wash-

ington has piled new responsibilities onto the SEC as a consequence of Dodd-Frank. I remain concerned, however, that the SEC has not made the necessary changes to its internal operations and structure or prioritized much-needed technology upgrades to oversee our capital markets.

Additionally, it is important that we ensure that the SEC is committed to completing the rulemakings required by Congress on time, such as those implementing the JOBS Act. I think that we can all agree that properly functioning capital markets will lead to the real jobs that Americans need, that people in my Virginia district need.

I would like to thank you again for your appearance here.

Thank you, Mr. Chairman, for holding this hearing, and I yield back my time.

Chairman HENSARLING. We have no additional opening statements, so today we welcome the Chairman of the Securities and Exchange Commission, Mary Jo White. She was sworn in as the 31st Chair of the SEC on April 10th of this year, so she brings all the wisdom and insight of 36 days of being on the job to our committee today.

Most recently, she has served as the chair of the litigation department of the New York law firm of Debevoise & Plimpton. Before that she served as the U.S. Attorney for the Southern District of New York from 1993 to 2002, where she oversaw the prosecutions of John Gotti, as well as the defendants responsible for the 1993 World Trade Center bombing.

Born in Kansas City, Missouri, she received her law degree from Columbia Law School, and she has a Masters in Psychology from The New School for Social Research, and a Bachelor's degree from the College of William and Mary.

Chairman White, welcome to the committee for your first appearance. I feel quite confident it will not be your last. You will be recognized to give an oral presentation of your testimony. And without objection, your written statement will be made a part of the record. Once you have finished presenting, each member of the committee will have 5 minutes within which to ask questions.

I wish to alert all committee members that we have agreed to allow the Chairman to be excused at 1 p.m.

Chairman White, again, welcome, and please proceed with your testimony at this time.

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

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

Chairman Hensarling, Ranking Member Waters, and members of the committee, thank you for the opportunity to testify on behalf of the Commission regarding the agency's recent activities, budget request, and upcoming challenges. Let me say, I am very pleased to be back in public service and to be appearing before this committee for the first time. I look forward to working with you to advance the Commission's critical mission of protecting investors, facilitating capital formation, and maintaining fair and efficient markets.

As has been said, I have been Chair of the SEC for only a month, but in this short period I have been impressed by the commitment and expertise of my four fellow Commissioners and my colleagues across the agency. And I am committed to working tirelessly with them on behalf of investors and our markets.

I have also been struck by the massiveness and importance of the SEC's responsibilities. Our agency is responsible for implementing and enforcing the Federal securities laws, overseeing over 25,000 participants in the securities markets, and reviewing disclosures and financial statements of more than 9,100 reporting companies.

My written testimony details the extensive work being done in the divisions and many of our offices that is so critical to the savings of American families and the growth potential of American businesses. With the passage of the Dodd-Frank and JOBS Acts, the SEC's vast responsibilities have become greater than ever.

As I enter this job, a number of immediate priorities are clear. They include completing in as timely and smart a way as possible the rulemaking mandates contained in both the Dodd-Frank Act and the JOBS Act; further strengthening our enforcement and examination functions, thus bolstering investor confidence and the integrity of our financial markets; and fully understanding and providing expert oversight of today's complex and dispersed marketplace so that it can be wisely regulated, which will require investing in technology and expertise to keep pace with the markets we oversee.

Continued funding at the current level and the staffing it supports would present significant challenges as we attempt to fulfill these and our many other responsibilities. The agency's Fiscal Year 2014 budget request will allow us to add approximately 676 new positions needed to improve core operations and effectively execute against both existing and new responsibilities.

While our funding is fully offset by securities transaction fees, and thus will not impact the deficit, we understand we must seek to use appropriated funds as careful stewards in the most efficient and effective way possible. We also acknowledge the need for the agency to continue to enhance its effectiveness and efficiency.

In recent years, the agency has made significant strides to strengthen its examination and enforcement functions, improved its capacity to assess risks, enhanced its technology, and reformed its operations.

With this in mind, the Fiscal Year 2014 budget request would provide additional funding in the following key areas.

Expanding oversight of investment advisers: During Fiscal Year 2012, the SEC was able to examine only about 8 percent of registered advisers. Significant additional coverage is essential if investors are to be appropriately protected.

Bolstering enforcement: it is important that we continue to send a strong message to would-be wrongdoers that misconduct will be swiftly and aggressively punished.

Hiring additional economists to support economic analyses in connection with Commission rulemaking and risk analysis.

Building oversight of derivatives and clearing agencies: two facets of our Dodd-Frank mandates.

Enhancing reviews of corporate disclosures, including staff to review draft registration statements submitted by emerging growth companies under the JOBS Act.

Investing in technology, a need that in my view cannot be overstated. While the SEC is rapidly modernizing our systems, significant investments are needed to properly oversee the markets and entities we regulate including improving our IT security and building data analysis tools.

And finally, enhancing training and development programs to increase our expertise and help maximize our efficiencies.

Thank you for inviting me to be here today to discuss the SEC's many initiatives. 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 improvements the agency has made to date.

I would be happy to answer any questions that you may have. Thank you.

[The prepared statement of Chairman White can be found on page 55 of the appendix.]

Chairman HENSARLING. Thank you, Madam Chairman.

The Chair will now recognize himself for 5 minutes for questions.

Chairman White, you can probably appreciate this, but having been in office for 10 years, I have yet to meet a head of a government agency who did not ask for more resources. So, you are certainly not atypical in that respect.

But the questions we have—a number of which obviously clearly predate your tenure—deal with the challenges with which your agency is faced. Is it a question of competence, is it a question of priorities, or is it a question of resources?

Many of my colleagues will be speaking more to these issues, but with respect to priorities, as you probably noted throughout my opening statement, I still have concerns, as do many, about the SEC devoting resources to a discretionary rulemaking dealing with corporate political reporting.

So the first question I have is, do you believe the SEC should require disclosure of items that are not material under Rule 10b-5?

Ms. WHITE. I think the answer to that is that the SEC does have authority, certainly with respect to line item disclosures, to require them if they would be helpful and important to investors. But plainly, the core of required disclosures is what will be material to investors.

Chairman HENSARLING. Okay.

Let me ask you this, Madam Chairman. Okay, the bulk of it is material, but you may require disclosure of items that are immaterial. But doesn't the SEC have to demonstrate materiality in order to bring a 10b-5 enforcement action? And if so, what is the point of adopting reporting rules if you cannot enforce them?

Ms. WHITE. Certainly in a 10b-5 action, the SEC would have the burden to prove materiality. You can have compliance infractions and violations that don't have materiality as an element.

Chairman HENSARLING. Okay. Let us look at materiality then.

Is it, in your opinion, material where—from what source a public company buys its coffee? Rainforestconcern.org has alleged that

many public companies are helping destroy rainforests by their selection of coffee.

Is that material?

Ms. WHITE. I know that is an issue that presents itself in some of our disclosure rules that are under litigation now, that were actually mandated by Congress.

It is a very fact-specific analysis. As you stated, depending on the company circumstances, I don't hear materiality in what you are stating.

Chairman HENSARLING. Let me try another one.

Is it material whether a company chooses to lease office space to an abortion clinic? Is that material?

Ms. WHITE. It is a fact and circumstances analysis to determine materiality. And so, you would have to look at all the facts with respect to that particular company in that particular situation.

Chairman HENSARLING. I am not really hearing an answer in there, Madam Chairman. But my thought process was or my understanding was that materiality is relevant to the investor. And I am just somewhat curious about rules that potentially could be adopted that really accommodate kind of the infinite and diverse political views of our Nation. And at a time when most of my constituents care about whether or not their investments will help them pay their increased health care premiums or help send a kid to college, I am not really sure that they want their SEC engaged in what they believe to be political policy.

And let me ask you this, Madam Chairman. Do you have any concern that it would undermine the credibility of your agency if there was a public perception that the agency was engaged in partisan political rulemaking?

Ms. WHITE. I think any government agency always has to be wary of, aware of the perception that it may be acting for political purposes, or any purpose other than fulfilling its core mission.

I am a very—for good or ill—apolitical person, and a very independent person. And my intention in running the SEC as Chair is to do the best job I possibly can in fulfilling that mission. But the answer—

Chairman HENSARLING. I'm sorry. My time is drawing to a close. I realize you have been on the job for 36 days, but are you aware if the Office of Management and Budget (OMB) has contacted you or anyone at the SEC regarding the SEC's Reg Flex agenda which, as you well know, recognizes your rulemaking priorities? And if so, have individuals from the OMB expressed an interest in seeing the potential rulemaking regarding political reporting moved forward?

Ms. WHITE. I am not aware of any such contact, Mr. Chairman, or any such view being expressed to the SEC.

Chairman HENSARLING. Okay. I would respectfully request that when you return to the SEC, you ask the question and present the committee with an answer.

[The information requested can be found on page 110 of the appendix.]

The Chair now recognizes the ranking member for 5 minutes.

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

As I referenced in my opening statement, my concern about cost benefit analysis, and the court case relative to the use of proxies to nominate to boards, I am very, very worried that this is going to be a tactic that will be employed over and over again in order to try and impede the SEC's ability to do its work.

We are aware, of course, of that case relative to the proxies, but there are two other cases that have already been brought to the court. I suspect there will be more. And I am worried about the costs.

I don't know what the cost of litigation was in the proxy case. And I don't know what the cost of litigation may be in the two cases that are before the courts. But do you see this as another way to have to spend precious resources that could be going to rulemaking if you end up having to fight all of these court battles?

Ms. WHITE. Clearly, any activity that occupies you significantly costs more resources, including litigation.

I do believe in the importance of robust economic analysis with respect to our rulemaking. My predecessor issued guidance to enhance the SEC's work in that arena in March of 2012. I think that is very important analysis to the rulemaking. Obviously, it is our responsibility also to make certain that our rules withstand a judicial challenge.

We need to be sure that we are being efficient as we do the economic analysis and we do the litigation so that it doesn't prevent us from doing necessary rulemaking.

Ms. WATERS. Oh, good. I guess we agree, as any reasonable person would, that it costs money to fight these battles in court.

Ms. WHITE. No question about that.

Ms. WATERS. And that takes away from your budget?

Ms. WHITE. No question that is part of the budget consumption, yes.

Ms. WATERS. Added to that, there is a bill that will be on the Floor tomorrow, H.R. 1062, the SEC Regulatory Accountability Act, the cost/benefit analysis bill.

There is a requirement in H.R. 1062 that the Commission revisit all past rulemakings 1 year after enactment, and every 5 years thereafter. To me, this seems like an unreasonable requirement, particularly when we consider that you would have to revisit longstanding provisions in our securities laws dating back to the Great Depression.

I would like you to comment on this. Is this reasonable? How do you envision being able to do that?

Ms. WHITE. I am familiar with the bill. And as I said before, I am a firm supporter of rigorous economic analysis. I do have concerns about this bill in terms of our being able to carry out our rulemaking function expeditiously and to provide market participants with certainty.

I think, at least as I read it, it would add additional new requirements to the SEC's economic analysis, the one you mentioned being one that is particularly of concern to me—the retrospective review that would need to be done after a year and then every 5 years under various criteria.

First, that sort of pops out to me as creating uncertainty for the market, and putting the rules under kind of constant challenge. I

guess I would add, though—and I go back to how committed I am to both the guidance that my predecessor issued—but robust economic analysis throughout everything we do, frankly, at the SEC, not just the rulemaking, and we have enhanced that function.

We have recently actually been, praised may not be a word you use here, but we have gotten positive comments from the GAO and the Chamber, as well as a recent comment on our cross-border rule about how well and robust the SEC is doing with respect to economic analysis.

I think we have to take great care that we don't impose additional requirements. I think these would provide at least the basis for a lot of challenges in court. Obviously, the rules should be subject to valid challenges, but that would create a lot of litigation that I think would undermine our ability to do our job.

Ms. WATERS. Thank you, Madam Chairman. And in addition to my concerns about the cost and the time and the burdens that are being placed, I am taking a look at H.R. 1062. In your opinion, does this legislation appropriately balance investor protection with other missions of the Commission such as capital formation?

Ms. WHITE. I think our mission is the tripartite mission we have all been talking about and reciting. And it is not just a mantra. I think you do have to sometimes effect a balance. I don't think they should be in conflict with each other.

I think what you would end up with here is an inability to—it doesn't just apply, as I read the bill, to rulemaking, but also interpretive guidance of various kinds. I think it would end up hampering us in our mission to fulfill our duty to investors, but also capital formation and the functioning markets.

Ms. WATERS. Thank you very much.

Chairman HENSARLING. The time of the gentlelady has expired.

The Chair now recognizes the gentleman from New Jersey, Mr. Garrett, for 5 minutes.

Mr. GARRETT. I thank the chairman.

Going back to my opening statement, discussing the ongoing concerns being raised by the American public about this Administration's attempt to bully organizations and groups that disagree with them politically, and in light of the chairman's comments with regard to some specific examples, can you commit formally today on removing the mention of a corporate political disclosure requirement from your Reg Flex agenda?

Ms. WHITE. Mr. Chairman, I think—my response to that is essentially, the petitions for requiring the political contributions are being reviewed in our Corporation Finance Division. That review is not completed. I can't prejudge the issue until I am the beneficiary of that analysis.

No one is working on a proposed rule now, and the Reg Flex agenda, I think, will come to me somewhat later in my tenure than today.

Mr. GARRETT. And just to spend 10 seconds on the examples that the chairman raised, I think your response was first, the difference between materiality and important. And second, you said these would be fact-specific to a particular company?

Ms. WHITE. Materiality tends to be fact-specific.

Mr. GARRETT. But any rule that you would promulgate, if you were to adopt any of those, as the chairman was suggesting, would not be for a specific company. It would be for all public companies, would it be not?

Ms. WHITE. That is correct, and the petitions do make the argument that such disclosure would be material—

Mr. GARRETT. Right. And—

Ms. WHITE. —across companies. But I get your point.

Mr. GARRETT. —the three main core missions of the SEC are what? Protecting the investors, ensuring orderly and fair markets, and facilitating capital formation. Using those as your core missions, do any of those examples that the chairman just gave you fall into any of those categories? Facilitating capital formation? Fair and orderly markets? Protecting investors?

Ms. WHITE. Those arguments, as I understand it, have been made in the petitions. I don't think it would be appropriate for me to comment and prejudge those arguments until I have gotten the staff's briefing.

Mr. GARRETT. Okay.

With regard to—I will just say it—with regard to economic analysis, your predecessor issued a memorandum last March providing guidance to SEC staff on economic analysis and SEC rulemaking. She indicated that this guidance was binding for SEC staff.

Have you also indicated to your staff—do you believe this guidance is also binding on them, as well?

Ms. WHITE. Yes, and I fully support it. And my understanding is that it is being followed, since my predecessor issued the guidance to the staff.

Mr. GARRETT. Without objection, I ask unanimous consent to put the prior memo from March 16th in the record.

Chairman HENSARLING. Without objection, it is so ordered.

Mr. GARRETT. Thank you. With regard to equity market structure, I know that we just had this roundtable, and that was good, a lot of back-and-forth. There seemed to be unanimity in certain areas where we could go forward on this.

Do you agree that the SEC should conduct a comprehensive review of the equity market structure regulatory regime?

Ms. WHITE. I think there is no question about that. We did issue the concept release on the equity market structure in 2010.

Mr. GARRETT. Right.

Ms. WHITE. And that work is actually continuing in that direction, to do that comprehensive review.

Mr. GARRETT. Okay. But that one was not truly a comprehensive review back in 2010.

Ms. WHITE. Essentially, lots of comments came in. There was a lot of work done. The Flash Crash happened. Dodd-Frank happened. There was a slowdown of that review.

However, it has continued, and is reaching the point where it is yielding some data and analysis that I think will be very useful. But certainly, it does recite that it is a comprehensive review of those issues.

Mr. GARRETT. Great. And just yesterday, thank you, I had the opportunity to be at the rating agency roundtable that you had. Do you believe that the SEC should finalize—as I pointed out in my

comments there—Section 939(a), before moving forward what I believe is really an unworkable and unwise idea of having the government select rating agencies or establishing a new or rotating formula?

Ms. WHITE. We have obligations under 939(a) and 939(f). But I am committed to—

Mr. GARRETT. But you would do 939(a), which is basically the first, before we get onto the start of the beginning of the alphabet, before we go down to the rest of it?

Ms. WHITE. I haven't—and I really can't commit to sequencing. I understand the importance of 939(a). It is something we need to carry out.

Mr. GARRETT. The importance of it is that it is mandatory, and later on it is discretionary, right?

Ms. WHITE. And—I am sorry. Later on?

Mr. GARRETT. Yes—

Ms. WHITE. We are required to do the study we are doing now. Yes. In that sense, it is not discretionary. But obviously, we make a decision as to what to do following the information that came in, including at that roundtable.

But what I am trying to do with all these rules and these rulemakings, is to make sure that we have the bandwidth so that one doesn't detract from the other.

Mr. GARRETT. And the last question with regard to the CFTC, I appreciate what you are all doing over at the SEC. The CFTC is working at a different pace than you are.

Are you committed to sitting down with CFTC Chairman Gensler to see if you can actually get it done jointly, since there is no benefit in having you working at cross purposes? That is a yes or no, I guess?

Ms. WHITE. We are totally committed to that. There have been a lot of discussions, prior to my arrival as well. But we are totally committed to that.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentlelady from New York, Mrs. Maloney, for 5 minutes.

Mrs. MALONEY. Thank you. During your confirmation hearing in March, you indicated that one of your highest priorities would be to further strengthen the enforcement function of the SEC in a way that is "bold and unrelenting."

Your predecessor had the same concern. In fact, one of the last letters that Chairman Schapiro sent was to Senator Reed, saying that certain statutory changes could enhance the effectiveness of the Commission's enforcement program.

I would like unanimous consent to place former Chairman Schapiro's letter in the record. I think it is an important letter. And—

Chairman HENSARLING. Without objection, it is so ordered.

Mrs. MALONEY. Thank you. It is my understanding that under the statute, the SEC cannot collect an amount equal to what investors actually lost as a result of a finding of abuse.

Can you comment on the limitations of the SEC on penalties? Can you comment on your feelings? Do you share her concerns? What actions do you intend to take in this area?

Ms. WHITE. I totally share the concerns. I think one of the most important things you do in a law enforcement agency, which the SEC is, is to have a strong enforcement arm that is a deterrent, not only to the individual committing the instant violation, but to those who might be thinking about committing violations in the future.

And the SEC's penalty structure doesn't allow, I don't think, a meaningful penalty in many situations, even in the case of the most serious offense or in the case of a recidivist.

We can't, for example, pitch a penalty to the amount of investor loss, which tends to be the big number in the big frauds, and we should do that. We don't have enhanced penalties for someone who commits a more serious violation 3 or 4 or 5 times.

And so, I fully support former Chairman Schapiro's request for legislation. I also support the bill that has been introduced to try to give that to the SEC.

Mrs. MALONEY. What other ways do you see the SEC strengthening enforcement in addition to penalties? What other ways do you intend to enforce measures?

Ms. WHITE. As we speak, essentially I am undertaking a review with the enforcement division of their various practices and policies to see if we can, in effect, enhance their ability to more efficiently go after the most serious wrongdoers up the chain, if the evidence goes up the chain, and to look at the settlement policies, as well as their capacity to litigate.

I think one thing that needs to happen at the SEC, and actually in our current budget request for enforcement, we are seeking 131 new positions, many of them for litigation and trial work, which I think we very much need to have.

Mrs. MALONEY. In terms of a global marketplace, which we have, what powers does the SEC have to enforce our laws and rules and regulations in a foreign country?

Ms. WHITE. We don't have powers to enforce in a foreign country. It is a global market. We certainly have global frauds that we have jurisdiction over to bring enforcement action against—again, depending on what the facts are, what the involvement of U.S. players are, but if you have a completely foreign company, a foreign national who commits a fraud, certainly in the United States, is the simplest example, we can proceed, and do proceed, against foreign nationals.

We also have in our regulatory powers the ability to deal with, for example, foreign issuers who don't play by the rules. We have a lot of initiatives going on, for example, and enforcement actions included involving CEOs in companies in the People's Republic of China, as one example.

Mrs. MALONEY. What about foreign subsidiaries that are connected with our financial institutions? Again, the enforcement powers in those situations?

Ms. WHITE. It will depend on what the facts are in a particular enforcement matter as to what you can do with respect to the foreign subsidiaries. You certainly don't have the power to go into another country and enforce our laws against a foreign subsidiary in those countries.

You also do get into difficult issues with respect to getting documents in the United States when you are investigating a global institution that has a foreign subsidiary.

Mrs. MALONEY. My time has expired. Thank you.

Chairman HENSARLING. The Chair now recognizes the gentleman from California, the vice chair of the committee, Mr. Miller, for 5 minutes.

Mr. MILLER. Welcome, Chairman White. It is good to have you here. I have somewhat of a concern on overreach that the chairman mentioned in his opening statement on the intent behind the Volker Rule as it prohibits insurance depository institutions' affiliates from engaging in proprietary trading.

And the statute specifically prohibits trading by an insurance business for the general account of the insurance companies, 619. I believe you are familiar with that. The proposal prevents the very trading, though, that Congress allows. Before you have an insurance company that happens to have a holding of a minor, small bank. And now those banking rules are being applied to the insurance company.

Your predecessor stated in March that the SEC was looking at whether there would be flexibility on this point. What is your position at this point on the rule?

Ms. WHITE. If I caught the full range of your question—

Mr. MILLER. Do you want me to restate it? Insurance company during their normal frame of business, they have a minor holding in a bank.

Ms. WHITE. Right.

Mr. MILLER. Now, those banking regulations are being applied to the insurance company.

Ms. WHITE. And we are very focused on that issue as we go through this rulemaking, and fully take the point.

Mr. MILLER. Do you agree with your predecessor? Section 13 of 619 is very clear. And my concern is that the perception on the street is that you are moving in a different direction. And I hope you are a breath of fresh air on this issue.

Ms. WHITE. I don't think that is the case. But if we need to say something more that we can say at this point, given that we are in the midst of the rulemaking, perhaps we should, and I will review that.

Mr. MILLER. Okay. Daily Average Revenue Trades (DARTs) are another concern. Regulators around the world are looking at U.S. markets and expressing concerns over high-level DART trading. Three years ago, the SEC put out a concept release on the market structure, but has not acted in any way on the items they proposed.

I understand you are only a month on the job, but where do you think you will see some of these changes occur in the area?

Ms. WHITE. I think, if you are talking about the concept release in 2010 on the equity markets, that is an extremely high priority to complete, to continue. It is something that did get delayed by the press of other business, but it has proceeded in the last 2 years, and it is nearing a place where I think we are going to be getting very useful data and analytics that will be very helpful to those issues.

Mr. MILLER. Okay—conflict minerals, I am assuming?

Ms. WHITE. I'm sorry.

Mr. MILLER. Conflict minerals?

Ms. WHITE. Yes.

Mr. MILLER. We are all concerned about what is happening in the Democratic Republic of Congo, but if you believe in a rule of law, you are innocent until proven guilty. If you look at the way that is being applied—and I know this is not an expertise of the SEC, and I don't think you should even be involved in this, but the problem is, you have businesses out there having to prove that there are no conflict minerals in their product, and if you can't prove it, you are found guilty at that point. And your mission is to protect investors, maintain fair, orderly, and efficient markets, and capital formation.

The SEC has little or no experience in crafting trade sanctions. Yet, that is the position you have been put in. And the burden on American businesses is huge. There is not even an exemption for recycled material.

But if you look at the application of the rule in the guidelines, we are impacting a huge sector of the African continent rather than dealing with the specific problem. What is your opinion on that issue, and how could you see us going forward in a more favorable direction, or at least a direction that is more fair to American businesses?

Ms. WHITE. I appreciate the question. That is one of the congressionally mandated rulemakings that the SEC was required to make. We certainly got a lot of comments along the same lines as yours. Again, this does precede me, but my understanding is that the staff, particularly of the Division of Corporation Finance, took great pains to try to reduce the burdens, but still be true to the statutory language and objective.

Some of the issues—this rulemaking has also been challenged. It is currently under challenge in the D.C. courts, and those issues have been raised there as well.

Mr. MILLER. I know you are very busy. It has been a tough 30 days, but I would like to see you do a few things: conduct a brief review of a small-business impact, and publish that study so we can actually review it; provide a means of minimizing eliminating unnecessary costs and burdens upon small businesses, which today they are very, very heavy on the business sector; explore innovative means of meeting the intent of exempting recycled material might be one way of doing it, because I don't believe anybody can find a source of recycled material.

Create a safe harbor that allows public companies to exercise reasonable due diligence. And I think reasonable due diligence is most important, and provide measures to reduce potential liability for public companies. You have General Motors, or Boeing, that might have a million different parts, or a million different contractors, and the liability falls back on them. I would like to see you do something in that area.

Chairman HENSARLING. The time of the gentleman has expired. The Chair now recognizes the gentlelady from New York, Ms. Velazquez, for 5 minutes.

Ms. VELAZQUEZ. Thank you, Mr. Chairman.

Chairman White, to better oversee the emerging crowdfunding industry, and prevent instances of fraud, the JOBS Act requires anyone acting as an intermediary to register with the appropriate self-regulatory organization as well as the SEC. How will this added layer of SEC oversight better protect investors?

Ms. WHITE. I think you mentioned two of the safeguards that are in the crowdfunding legislation and structure. The funding portal and the self-regulatory organization are very important to seeing to it that when we do actually do the rulemaking in that arena, investors are protected. The SEC always has to be focused on maximizing investor protection wherever it can be. Those are safeguards in that legislation.

Ms. VELAZQUEZ. I am concerned about the likelihood that two regulators will create confusion and drive up costs, regulatory costs for small businesses. What is your take on that?

Ms. WHITE. The SEC is, and certainly I personally am very focused on small businesses and their ability to more easily raise capital. Some of the market structure issues relate to that as well. And in terms of inconsistency between regulators in the same space, the goal should be for consistency.

Ms. VELAZQUEZ. We are starting to hear from most Federal agencies about the impact that the sequestration is having on their day-to-day operations. And I would like to ask you, what effect, or what impact is sequestration having on the SEC's ability to implement the Dodd-Frank Act and the JOBS Act?

Ms. WHITE. There is no question that it is having a significant impact on the SEC, although to credit our financial management folks in particular, I think the SEC anticipated well and planned well for the possibility of sequestration. And so, I don't think we will have furloughs, for example.

But we certainly have had to slow investments in various IT initiatives that are important to enforcement and examination. We have also had to delay hiring to build out the staff we need for the new responsibilities under Dodd-Frank.

Ms. VELAZQUEZ. Beyond sequestration, what effects will further reductions in your budget have on rulemaking and enforcement?

Ms. WHITE. I guess everyone who comes says this, but I am struck by the massiveness of our responsibilities, and the need for, certainly, the funding that we have sought in this budget.

I think the independent consulting group that actually reported to us per Dodd-Frank pointed out the gap between our funding and the ability to carry out our mission. We have tried to be surgical with respect to our request, and really to target the most pressing needs, but we need the funding.

Ms. VELAZQUEZ. Chairman White, the SEC has been criticized for the proposed rule on general solicitation, and advertising of private securities. Specifically, stakeholders have stated that the rule does not provide a proper mechanism for validating accredited investors, which will create confusion in the marketplace.

Do you expect the SEC to clarify this rule to help small companies verify which investors can invest in their securities and avoid unintentional violations?

Ms. WHITE. That, again, is among the many rulemakings that are currently under active discussion between the staff and my fel-

low Commissioners. We are very much aware of that issue as we go forward.

Ms. VELAZQUEZ. Thank you.

Thank you, Mr. Chairman.

Chairman HENSARLING. The Chair now recognizes the gentleman from Alabama, Mr. Bachus, our chairman emeritus, for 5 minutes.

Mr. BACHUS. Thank you, Mr. Chairman.

And it is "Chairman," Chairman White. The Senate confirmed you unanimously, and I think you come with eminent qualifications, and I think many of us were thrilled with your nomination.

And I want to just introduce in the record, Chairman Mary Jo White's biography, and invite all of the Members to read it. I think anyone who thinks she is going to be bullied probably has not read her biography.

She was the first woman in over 200 years to serve as the U.S. Atorney for the southern district of New York, and others have mentioned many of your prosecutions. They didn't mention the embassy bombings in Africa, which you successfully prosecuted.

Chairman HENSARLING. Without objection, that will be entered into the record.

Mr. BACHUS. Thank you.

The question of funding has come up this morning. We as a committee have urged you to do more economic analysis. You have the implementation of Dodd-Frank, which we described many times as one of the most massive statutes ever passed by this Congress.

You mentioned investor advisers, and we very much think that there ought to be more frequent examinations, as do you and your predecessor. Others have mentioned the JOBS Act and others so you have many other rulemaking responsibilities, and you are being asked to review existing statutes.

So you do have very much of an increased workload. And I do want to say publicly that I think it would be penny wise and pound foolish for there not to be some bipartisan agreement for a funding increase. And I would urge you to use the goodwill that you have with both the Senate and the House to be a catalyst for that.

Ms. WHITE. Thank you very much.

Mr. BACHUS. We have discussed this morning, the chairman and the subcommittee chair, political contributions and their disclosure. We have all kind of followed the IRS, and I think we are all very concerned with the constitutional rights to free speech, free association, the right to participate in the political process.

And I would urge you to look at—also, you mentioned investors. And I can't really see any more than maybe tenuous at the most, a remote, tie between the coordination of the SEC in disclosing this. And I think there may be some nebulous benefit.

The chilling effect on that, or the message it has sent would be serious. I would urge you—and I will note—I am not sure if anyone mentioned that the catalyst for this was, I think, 11 law school professors. And I think you will acknowledge they are not economists, they are not business people. They are not investing capital. They are not running companies.

They don't have a fiduciary relationship with the shareholders. And I also would ask you to respect State, corporate law, which you did as a U.S. Attorney. And also remember that there is the fidu-

ciary role of the board of directors as you move forward with that petition.

Ms. WHITE. I appreciate that. I take your points. I can't prejudge the issue, but I fully take your points.

Mr. BACHUS. Thank you. Governor Tarullo has talked about Section 165, that there may be inadequate capital standards for broker-dealers, and I am not going to again ask you to pre-judge that. But I see that as a usurping of the SEC's authority by the Federal Reserve.

And I see nothing in Dodd-Frank Section 165 that allows them to do that. I am going to give you a letter that I wrote to Chairman Ben Bernanke, and I really pointed out four reasons why I believe the Fed is wrong on this issue.

Probably the most important is that our national treatment of foreign broker-dealers, and foreign financial institutions has always been evenhanded with our domestic institutions. And as you know from being in New York, it is very important that we are even-handed in that regard. So I am going to introduce this for the record, and I ask you to—

Chairman HENSARLING. Without objection, it is so ordered.

Mr. BACHUS. —defend the SEC's jurisdiction.

Ms. WHITE. I appreciate that.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from North Carolina, Mr. Watt, for 5 minutes.

Mr. WATT. Thank you, Mr. Chairman.

And thank you for being here, Madam Chairman. I have, over the last month or so, started having a greater degree of empathy toward regulators who have come before the committee.

[laughter]

Ms. WHITE. It is a dying breed, right?

[laughter]

Mr. WATT. So, I have a couple of softball questions to—

[laughter]

Ms. WHITE. Good!

Mr. WATT. —pose to you.

Ms. WHITE. Can I say, yes now or—

[laughter]

Mr. WATT. Seriously, a month or so ago a number of House and Senate Members sent a letter to the SEC about the question of pre-dispute arbitration agreements, that broker-dealers and investment advisers are entering into with customers. And the SEC has the authority under Section 921 of Dodd-Frank to promulgate some rules about this.

Because of my service on the Judiciary Committee, I am a little concerned that these supposedly voluntary agreements are not so voluntary at all. And that they often restrict access to participating class actions, for example, and things of that sort.

So I wanted to see whether you think that is an issue and whether the SEC is planning to promulgate rules, and if so, when that might occur? Is it a high priority issue for the Commission?

Ms. WHITE. It is one that is under—I guess active work is the right term.

The SEC has not made a decision whether to exercise its discretionary authority in that space. It has gotten a lot of pre-proposal comments on it, lots of discussion on it, with both sides represented in that discussion.

Recently, I think on March 1st, if I am remembering correctly, as part of a request for further public information on the standards that ought to apply to brokers and investment advisers, legal standards and also just possible harmonization of those regulations, one set of those questions to get information for the staff was addressed to the various alternative dispute resolution mechanisms that are used by both the broker community as well as the investor advisory community.

So that is something that will be coming in shortly and then we will review that and proceed to figure out what to do about it, but no judgment has been made yet.

Mr. WATT. Thank you. I am glad that you all are looking into that in a very balanced way.

And, Mr. Chairman, I think I will yield back the balance of my time without treading into any additional territory here.

[laughter]

Chairman HENSARLING. No additional territory tread on in the last minute, 36 seconds.

The gentleman from New Mexico, Mr. Pearce, is recognized for 5 minutes.

Mr. PEARCE. Thank you, Mr. Chairman.

And thank you, Madam Chairman, for being here today. A Wall Street Journal article from August 25, 2011, discusses the SEC questioning oil and gas companies about fracking.

And the SEC's comments in that article—and, Mr. Chairman, I request unanimous consent to place this article into the record.

Chairman HENSARLING. Without objection, it is so ordered.

Mr. PEARCE. In the article, the SEC is saying that the questions are directed to minimize the environmental impact and that is according to copies of the letters that you all sent.

And so my question is, under your watch, are you going to continue asking such questions?

Ms. WHITE. That is an area I have to say that I will probably have to get back to you on. I am not familiar with what the history on that has been and I certainly would commit to get back to you on that.

Mr. PEARCE. I appreciate that, but in the hearing on September 15, 2011, the SEC Chairman promised to get back to me on at least five different things and I am still waiting. My ears are just delicately waiting for even a phone call.

Ms. WHITE. Just hold me to it. I will get back to you on it very promptly.

Mr. PEARCE. Okay. Is it possible that we might deal with some of the questions that were raised in this hearing on September 25, 2011?

Ms. WHITE. I haven't seen what that is—

Mr. PEARCE. No, I understand.

Ms. WHITE. But yes is the—

Mr. PEARCE. Yes, they—track along the same way.

Ms. WHITE. I will look at—

Mr. PEARCE. They track along the same way.

So basically, this idea that the SEC is interested in what people are doing to mitigate environmental impact is a curious thing. I can understand the rationale because if you are messing up the environment, then you will be subject to lawsuits or fines or something which would affect the stock price, so I follow the rationale.

One of the other questions I am sure you will have to ask the system, but have you ever asked anything with regard to the killing of bald eagles or other migratory birds?

We have two acts, the Migratory Bird Treaty Act and the Golden and Bald Eagle Protection Act. So my question is, I know you have asked questions on fracking, but have you ever asked any company regarding wind energy if they are involved in the killing of these species?

Ms. WHITE. Not that I am aware of, but—

Mr. PEARCE. But you see the discontinuity—

Ms. WHITE. Yes, I take that point.

Mr. PEARCE. That you have an interest in the environmental impact, and with the things that are happening in the IRS right now, it gives one pause to ask if you are only concentrating, in the SEC, on those conservative organizations.

Are these Nixonian tactics spreading across from the IRS to you? The Fish and Wildlife Service has yet to convict anyone. BP paid $100 million in fines for killing birds in that spill. Exxon killed 85 birds and paid a $600,000 fine, but this Administration is doing zero.

They haven't fined any wind companies and the estimates are that the wind companies kill 530,000 birds a year. And in fact, the golden eagle is diminishing in population in parts of California because of the wind generators, and so your agency has been asking questions, and I will take it that it is your responsibility. But if your agency has not also been asking questions—to protect the environment and protect the species of other laws, then I think that we have a right to question whether or not your agency is being used as a political tool by the Administration the way that other agencies appear to have been used.

And we look at the AP scandal. This Administration is appearing to get a scandal a day. But please understand that if you are going to question one group of companies on their environmental impact, you must also ask the other side of the political equation, if there is a political equation business, about their environmental impact and their impact on endangered species.

Does that seem credible?

Ms. WHITE. Clearly, I need to look at the specifics of these particular issues, but I will say this. The SEC is an independent agency. I think—

Mr. PEARCE. The IRS is, too. We have been told that in the press in just the last couple of days.

Ms. WHITE. And my experience with the SEC over my career has been that it is a very apolitical agency. I have no reason to think they are not on this, although I obviously am going to look into these specifics.

And I can also assure you that I am—

Mr. PEARCE. —my time has lapsed—

Ms. WHITE. —that I am also—

Mr. PEARCE. Before it lapses, Mr. Chairman, I request unanimous consent to put this other article from the Dispatch in the record. I will submit that.

Chairman HENSARLING. Without objection, it is so ordered.

Ms. WHITE. And I would just add that I am a very, very independent person, also.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from California, Mr. Sherman, for 5 minutes.

Mr. SHERMAN. I stopped reading science fiction when I got to Congress because in my work I found more strange and wonderful things than could be in the pages of science fiction.

I want to discuss with you a little bit the proposal for disclosure of political expenditures.

You have been called upon by the Chair of the relevant subcommittee to resist outside political pressure, refuse to be bullied, and to demonstrate the SEC's independence by immediately exceeding to the demands of the Chair of the relevant subcommittee and the full committee.

[laughter]

We have been told that there is a constitutional right of corporate CEOs to use other people's money, in this case the shareholders, on political communications or propaganda without even disclosing what they are doing.

This is, of course, the strangest of all constitutional rights since it is vested only in corporate CEOs. None of my constituents whom I know well have the authority to spend other people's money on political communications.

Now, if indeed we do have these disclosure requirements, it is critically important that they be impartial.

Could you imagine any draft emerging from the SEC that would impose one kind of disclosure requirement on, say, Koch Brothers Industries and a different disclosure requirement on, say, Berkshire Hathaway or Ben and Jerry's? Or would the regulations be even-handed regardless of which corporation was involved?

Ms. WHITE. Again, I emphasize there isn't a current proposal.

Mr. SHERMAN. Right.

Ms. WHITE. We don't have a recommendation even from the division as to whether or not to recommend the rule proposal. But if you are talking about required disclosure on a particular subject, that is generally applied uniformly.

Certainly, you don't make distinctions on any factors you shouldn't be. Sometimes, you will have scaled disclosure for smaller companies and things like that, but—

Mr. SHERMAN. But not a requirement that a corporation must disclose its conservative expenditures and ignore its liberal ones.

I would point out that materiality is what is of interest to investors and not all investors focus exclusively on earnings per share.

We already require the disclosure of executive pay, of involvement in terrorist countries, in the conflict diamonds, and now millions of Americans, all of them potential investors or investors through their pension plan want to know about these political ex-

penditures. I hope you will, when you come before us next time, be able to report that this process has gone forward.

Another process that should go forward is the Franken-Sherman Amendment dealing with credit rating agencies. Many have pointed to the fact that they gave AAA ratings to junk bonds as the cause of the great calamity that hit us in 2008.

Congress, in the law that was signed in July 2010, required the SEC to either implement the Franken-Sherman solution or to come up with a better one. You have done neither.

I would hope that next time you come here, you will be able to say that you adopted regulations consistent with the statue to provide for a panel to choose the credit rating agencies, especially for mortgage-backed securities, so that we end the process where the issuer selects the evaluator of the bonds being issued, which is like the umpire being selected by the home team.

And the one other thing I would want to mention—my time is going quickly—is that the FASB derives much of its power by the mandate of the SEC.

They are coming up with a draft regulation today which will substantially harm small business, which will throw a real monkey wrench in the real estate economy.

They had promised 67 Members of Congress who wrote them about this that they wouldn't adopt regulations which would have that effect. And I hope that just as we oversee you, you will oversee them.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Pennsylvania, Mr. Fitzpatrick, for 5 minutes.

Mr. FITZPATRICK. Thank you, Mr. Chairman. I yield my first 30 seconds to Mr. Garrett of New Jersey.

Mr. GARRETT. Thank you.

And just briefly, in retort to the gentleman from California, I wish to remind the gentleman from California that it is the Constitutional and legislative authority of this committee to have oversight of the SEC. When we direct the SEC to do something, we are doing so within our legal authority to do so.

That is not the case when outside organizations are using bullying techniques against the organization, and it is not the case when this Administration exerts undue influence outside the normal channels.

I yield back to the gentleman.

Mr. FITZPATRICK. I thank the gentleman.

As a result of several factors like the U.S. credit downgrade, as well as the euro debt crisis, there was about $170 billion in outflows and money market funds during the summer of 2011. And I understand that some funds saw redemption request beyond 30 percent of total assets.

However, no fund broke the buck during this period, which seems to have been a good test for the effectiveness of the 2010 rule change' specifically, Rule 2a-7. The question is, how would you rate the performance of money market funds since the SEC's 2010 amendments, Rule 2a-7?

Ms. WHITE. I think that the 2010 reforms, which were designed to make them more resilient—the staff has done an economic study

of that particular issue, economic analysis of it, and I think the conclusion is that they are more resilient.

What the study also says, though, is that the systemic risks run on the funds concern, as we saw during the financial crisis, is not met, or was intended to be met, by those reforms, but certainly, I think they have done well.

Mr. FITZPATRICK. But do you support the study conclusion that the reforms—it is much less likely that a fund would break the buck?

Ms. WHITE. I think the—as I recall, what the study says is if the same stress that was apparent during the crisis was present, you still had that potential risk.

Mr. FITZPATRICK. On April 25th, when you spoke at the meeting of the FSOC, you told them—and this is a quote from that meeting—"I think it is important to move ahead with further reform of money market mutual funds." You said that you believed this reform would be best handled by the SEC.

Do you believe the SEC must act with new rules for money market funds in order to stave off some action from FSOC?

Ms. WHITE. I can't speak for FSOC. I can speak for myself and the SEC, that I think that money market funds are investment products. And if something more is to be done—and, indeed, I made a statement of FSOC that I am expecting that the staff will soon make recommendations to the Commissioner in this field that should be done by the SEC.

Mr. FITZPATRICK. Have you had time to review the extensive money market fund comment file at the SEC and FSOC? And is there still a possibility that after reviewing all the data, all the comment letters, that you will decide not to move forward with major changes in the money market fund?

Ms. WHITE. My statement at FSOC is still the current state of affairs, which is I think it is important to move forward with further reforms. All issues are currently under discussion between the staff and the Commissioners, but I do expect the staff and the Commissioners to be dealing with that in the near future.

Mr. FITZPATRICK. Ma'am, before I came to Congress, I was a local elected official in Bucks County, not far from the City of New York, and a lot of local officials and State officials rely on money market funds as a source of sort of cash management. It is an important tool to have in the toolbox.

Numerous municipalities and municipal organizations have written to the SEC and FSOC with concerns about how new regulations on money market funds would impact their costs of borrowing. If there were large outflows from the $2.7 trillion money market mutual fund industry, do you think that banks or other alternatives to money market funds would redeploy those assets to meet the needs of these municipal borrowers without imposing new borrowing costs on those municipalities or States?

Ms. WHITE. Let me say one thing that I think is very important, which is that there is no question about the utility of money market funds, both to investors and to those who borrow short term. And certainly one of our objectives in doing anything further at all would be to preserve the value of that product.

We also—and again, our economic study addressed this—you want to have a very careful eye on the impact of, where does this money go if it actually does leave the money market funds? You don't want it going into more systemically at-risk institutions. So, the staff and the Commissioners are very cognizant of those factors.

Mr. FITZPATRICK. So you will consider the cost on municipal organizations with respect to any reforms that are suggested or—

Ms. WHITE. We are considering all issues and all impacts.

Mr. FITZPATRICK. Thank you.

I yield back.

Chairman HENSARLING. I now recognize Mr. Green of Texas.

Mr. GREEN. Thank you, Mr. Chairman.

I thank Chairman White for appearing today. My understanding is, that has been codified, such that you are the Chair—

Ms. WHITE. I tried to call myself "Chair," but I was told I was violating the statute, so—

Mr. GREEN. Okay.

I want to accord you every respect that you have earned, and I greatly appreciate your appearance here today.

I do want to take just a moment to say to persons who may be viewing and to you that there is a spirit of bipartisanship that creeps into this committee from time to time. And yesterday was one such occasion when we passed the Homes for Heroes Act.

I want to thank the chairman of the committee, Mr. Hensarling, and the ranking member, Ms. Waters, because they were very instrumental in getting this done. I would also thank the staff, again, because without a great staff, you can't do great things, and they have done a tremendous job.

If I may, I would like to just visit with you about the budget, which is a part of the style of the hearing today. And I do want to mention to you that the President has asked for $1.67 billion.

My understanding is that these are not dollars that would come from taxes. The $1.67 billion would come from fees that are collected. And my question to you is, are the transaction fees and other fees sufficient to cover the $1.67 billion that has been requested?

Ms. WHITE. The answer to that is it would not have any impact on the taxpayers. It would be deficit-neutral. And I think it is approximately $0.02 to the $1,000 ratio—would cover it, is my understanding.

And obviously, you would also have the ability to charge a slightly higher amount if you needed to, but I don't believe that is necessary.

Mr. GREEN. And is it true—I believe you have said it, but some things absolutely require repeating—that the amount in question would not involve one cent, not one cent of tax dollars? Is this true?

Ms. WHITE. That is correct.

Mr. GREEN. Hence, the amount in question would not in any way impact the deficit? Is this true?

Ms. WHITE. That is right. It is deficit-neutral. No impact at all on the deficit.

Mr. GREEN. And notwithstanding the lack of impact of your request on the deficit, is it also true that you are subject to sequestration?

Ms. WHITE. Yes, we are.

Mr. GREEN. And is it true that you have not furloughed anyone thus far, but sequestration is having an adverse impact on your technology needs, your training needs, your contracts? In fact, you need to hire about 676 additional people. Is this correct?

Ms. WHITE. That is correct.

Mr. GREEN. And could you just explain for just a moment some of what you might do with the 676 new people? Let me just mention some of what I have been accorded.

I have an indication that you currently oversee about 35,000 entities, including 11,000 investment advisers, 9,700 mutual fund and exchange traded funds, and 4,600 broker-dealers with more than 160,000 branch offices.

I show that you have approximately 460 transfer agents that you have to work with at 17 national security exchanges, 8 active clearing agencies, 10 Nationally Recognized Statistical Rating Organizations (NRSROs), as well as the Public Company Accounting Oversight Board (PCAOB).

This is just a little bit of what you do. It appears to me that we need to make more of the fact that you do have a very large job to do, and we need to well define what you do. So, could you say just a little bit more about what you do and why it is so important that you get this $1.67 billion in fees, not tax dollars, and why it is so critical to the operation that you oversee?

Ms. WHITE. Yes. As I think I said earlier, one of the things that struck me in my first month here—and I have reviewed the budget request, I fully support it—is just how massive the responsibilities are of the SEC.

This budget request is, I believe, not only responsible, but surgical in many ways. It is essential for the SEC to be able to carry out its mission.

I cited one example on investment advisers. We would—

Mr. GREEN. Allow me to interrupt for just a moment and ask this quickly. Do you have an internal process by which you do this such that it is not done arbitrarily, capriciously, or willy-nilly?

Chairman HENSARLING. The time of the gentleman has expired. Chairman White can submit the answer in writing.

The Chair now recognizes the gentleman from California, Mr. Royce, for 5 minutes.

Mr. ROYCE. Thank you, Mr. Chairman.

And Chairman White, welcome.

I listened closely to your comments before the Appropriations Committee, stating that we must find common ground with our counterparts abroad, and nit together a regulatory network that offers protection, consistency, and stability to market participants.

On this subject, at a hearing in October 2011, I asked Secretary Geithner about the extraterritorial application of derivative rules. Specifically, his thoughts on whether a misalignment between U.S. and foreign jurisdictions on either timing or content could, as Fed Chairman Bernanke stated previously, cause a "significant com-

petitive disadvantage." Those would be Chairman Bernanke's words.

The Treasury Secretary agreed, saying—and I will quote him—"The Fed Chairman is right to point out that there are provisions of the law that, because of how they treat the foreign operations of U.S. affiliates, could cause that problem that we are worried about."

I assume you agree with Chairman Bernanke and Secretary Geithner about the competitiveness issues that could arise with cross-border application. Just maybe a yes or no on that, Chairman, if it is okay.

Ms. WHITE. I do agree with that. I think our rules are also quite robust as well.

Mr. ROYCE. I also asked then-Secretary Geithner about the divide between the CFTC and the SEC on timing and on content. And he asserted, and I will just go with what he said, "If you don't have alignment among them, then you are right to say how are we going to convince the rest of the world to come to a common standard?"

So these comments were 20 months ago, and still today, the CFTC and the SEC are not on the same page. One, yours, is conducting a deliberate process with a proposed rule versus rushed guidance and no-action letters, over at the CFTC.

We have heard from foreign regulators, both in testimony and in a recent letter, that the bifurcated U.S. approach is causing confusion, and putting us at a disadvantage. And I have a couple of letters here from The Journal today, "New U.S. rules hinder derivatives trading in Asia," and this is sort of a common theme that we see.

Briefly, do you agree that misalignment between the SEC and the CFTC is problematic, and would your preference be that the CFTC extend their executive order, which expires on July 12th, to avoid market uncertainty and avoid the confusion and measurable impacts similar to last year?

Ms. WHITE. I guess my first point is plainly, yes, consistency is an objective, I think of everyone, to avoid the issues that you are mentioning. We have been working with the CFTC and our foreign counterparts for quite some time, and we continue to do that as we try to fashion these rules. It is not required that they be joint, but plainly, it is extraordinarily important for the marketplace that we try to reach that common ground.

Mr. ROYCE. Thank you. I am going to ask you another question, because we are 5 years out from one of the biggest regulatory breakdowns in U.S. history, at least from the standpoint of Mr. Markopolos, who testified here, but I tend to agree with him on that. I think that the SEC's failure to detect the multi-billion-dollar Ponzi scheme run by Bernie Madoff was truly egregious.

And one of the takeaways from it, as he testified to us about the over-lawyered nature and the culture and the desire to get into the equation expertise with market experience, do you now have an adequate complement of staff at the SEC with market experience in investment and in trading? And do you believe having a workforce with deep knowledge of the inner workings of our capital markets will assist you as head of the SEC?

And lastly, among the recommendations of the Boston Consulting Group study required by DFA was that the number of offices and divisions reporting to the SEC Chairman be streamlined at present. Chairman White, you have 22 direct reports. Do you believe this is a structure that promotes efficiency? What will you do to address this? These were the other issues I was going to ask you.

Ms. WHITE. First, on the market-expert question, it is an extremely high priority of mine to see that we indeed—and not just in enforcement and the obvious divisions—throughout the agency, enhance the number of experts, economists, market experts, and traders that we need. Enforcement has done that since the Madoff situation.

Chairman HENSARLING. The time of the gentleman has expired. Any further answer can be submitted in writing.

The Chair now recognizes the gentleman from New York, Mr. Meeks, for 5 minutes.

Mr. MEEKS. Thank you, Mr. Chairman.

Thank you, Madam Chairwoman. Welcome. Congratulations to you, I think.

Let me ask you a question. Basically, Section 913 of the Dodd-Frank Act required the SEC to study the differences in the standard of care for investment advisers, the fiduciary standard and broker-dealers, the suitability standard, and provided the SEC with the authority to impose the fiduciary standard on broker-dealers.

Now, there was a staff report that recommended that the SEC consider rulemaking that would uniformly apply the fiduciary standard no less stringent than currently applied to investment advisers to broker-dealers.

My question is, how is the SEC taking into consideration the possibility of a likely impact on smaller accounts if brokers leave the marketplace or reduce the quality and depth of the services they provide? I am just concerned, if they just left the marketplace.

Ms. WHITE. If those rules were applied?

Mr. MEEKS. That is correct.

Ms. WHITE. I think one of the reasons—and again, this precedes my arriving at the SEC—but that the SEC decided to get additional information with respect to the business models, the market of brokers, and investment advisers was so that they would have that additional information before the SEC makes any decision on those issues.

Plainly, what you have seen in the marketplace, and the SEC has gotten data on this, is that retail investors can be confused as to whether they have hired a broker or investment adviser and don't realize the standards may be different and may mean something to them. And so, you obviously want to be very careful to protect those interests.

But on the other hand, you also want to take into account the different business models and to make an optimal decision. So no decisions will be made on this issue until that information comes in. It was put out for request on March 1st, and then the SEC staff will analyze that and make a decision.

Mr. MEEKS. Let me—and I appreciate that, and I applaud the SEC's approach because I think it has been careful, in particular, your decision to ask for the RFI to provide the information.

But you know that the Department of Labor (DOL) has indicated that it intends to fast-track a rule that would impose its own standard of care on brokers. And I am concerned that the DOL's fast-track approach will seriously undermine the kind of approach that the SEC has been going by, if not completely negated it.

And so I was wondering, does the SEC share any similar concerns?

Ms. WHITE. The answer is that the staff has been in very close contact, frequent contact with the staff at the Department of Labor as well to discuss the issues you mentioned, as well as others. Obviously, they are an independent different agency than the SEC. They have to make their decisions ultimately.

But one of the things we are certainly engaging in the dialogue for is to make certain that the differences in our space, and all the issues are on the table for them to consider as well. So, we are continuing those dialogues.

Mr. MEEKS. So you are having this kind of cross-dialogue with the DOL so that we could try to make sure that—I don't want the kind of confusion that would come particularly in regards to many of those that service IRA services, because then small folks—I know especially in the African-American community, if we we don't have those brokers, then they won't have the opportunity to invest.

And so, I don't want the complications or the confusion to cause individuals to leave the market, and thereby cause people not to be able to save for retirement.

Ms. WHITE. I take your point completely. And my understanding is that is part of the discussion. They will ultimately make their independent decision. But we are certainly informing them from our expertise and knowledge what the marketplace looks like, and what the effects could be.

Mr. MEEKS. Let me just ask another question that is off topic a bit. I am, as you know, from New York. And I am kind of concerned about our current market structure, when you talk about technology and the significant rise of what is called "DART trading" and fragmented liquidity. A lot of complexities, a lot of which I am just trying to figure out and understand as I talk to some of my folks.

But particularly, as it does erode the public price to help for smaller-cap companies—I am looking at the smaller-cap companies, and the effects that it has. So I am wondering—and I know that there are some programs or some pilot programs—I see I am out of time—that are being utilized and looked at. Is the SEC interested in looking at pilot programs or initiating pilot programs in that area?

Ms. WHITE. We recently had a decimalization roundtable that was directed to that, and there was enthusiasm for a pilot program in terms of what the spread should be, and how one might structure a pilot program.

All those views are being considered under discussion now between the staff and soon I think there are going to be recommenda-

tions made to the Commission. But certainly, we are always focused on small businesses and the small-cap companies as well.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Texas, Mr. Neugebauer, for 5 minutes.

Mr. NEUGEBAUER. Thank you, Mr. Chairman.

Chairman White, the SEC's mission is to protect investors, maintain fair, orderly, and efficient markets, and to facilitate capital formation. I think the Dodd-Frank Act has attempted to address the first two parts of that mission—investor protection and promotion of fair markets.

I am interested in hearing your perspective on what you think the role of the SEC is for capital formation, and how you see your tenure there facilitating that?

Ms. WHITE. First, it is a critical part of our mission. All parts of our mission are critical. But capital formation is certainly very much on my mind, and I think on the agency's mind.

At the moment where we are focused, in terms of the staff work, is predominantly on the JOBS Act and the rulemakings under that. Plainly, the objective of the JOBS Act is to facilitate capital formation.

I think before the JOBS Act was enacted, the staff was quite focused on a review of what one might do really across-the-board, across markets, to facilitate capital formation because that is what is critical to the health of the Nation. It is what is critical to the health of investors.

Mr. NEUGEBAUER. One of the things that I think sometimes the agencies do, is they are really good at waiting around for Congress to encourage them to do something, or in some cases, instruct them to do that or regulate that they do, or legislate that they do that.

Do you see yourself fostering an agency where you can see opportunities in the marketplace where you can sometimes streamline some of these processes, instead of waiting for us to ask you to do that? One of the things I get frustrated with is that the government is really supposed to work for the people. And certainly, making sure that markets are transparent and operate with integrity is an important part of that.

But the other part of it is this capital formation piece. Your predecessor came to talk about that. And we didn't ever hear much out of that.

Ms. WHITE. It is certainly my impression that the staff is quite focused on that. I certainly am quite focused on that.

I think one of the things that I actually think should be a priority—it is a priority of mine as an example—is to simplify, make more meaningful the disclosure requirements, not just for small companies, but for larger companies, so that we end up not having it be so burdensome, and perhaps make it more informative.

So that is an example. But it is our responsibility to stay focused on capital formation. And certainly during my tenure, we will.

Mr. NEUGEBAUER. So when are we going to finish the jobs?

Ms. WHITE. As promptly as I possibly can.

Mr. NEUGEBAUER. That is—

Ms. WHITE. I am a member of a 5-person Commission, but it is a high priority of mine to finish all of the congressionally mandated

rulemakings. And I am trying to provide the leadership at the Commission to do that.

Mr. NEUGEBAUER. I think we are disappointed, because I think we were all kind of excited that we actually were able to pass something, and then I think, the honeymoon has kind of worn off on that now, because there was a lot of excitement about that, because it had taken so long to get the wagon up and running.

Ms. WHITE. I appreciate that. There is excitement. I hope it is still out there, but I understand your point completely.

Mr. NEUGEBAUER. Section 939(a) of Dodd-Frank sought to end the Federal Government's apparent endorsement of credit rating agencies and investor overreliance on them by almost requiring every Federal agency to review any of their rules using credit ratings to assist creditworthiness.

The SEC has not yet completed its work to comply with Section 939(a). Nevertheless, the SEC announced on February 26th that it would convene a credit ratings roundtable, I guess, on May 14th—and I assume that already happened—to examine the feasibility of a system in which the public or private utility would assign credit rating agencies to determine credit ratings for structured finance products.

Do you believe that the SEC should reinsert the government into the rating business?

Ms. WHITE. The roundtable was to inform the staff and the Commissioners as to what judgments should be made in that space. In terms of the removal of the references, some have been done, but that remains as the priority as well.

But I can't really prejudge the assignment issue since we just received the additional information that the staff and the Commissioners had decided was needed in the roundtable we just had.

Mr. NEUGEBAUER. I think it would be interesting, it would be informative if you could kind of follow up with me on that after you have had a chance to debrief on that roundtable.

Chairman HENSARLING. The time of the gentleman has expired, and Chairman White can follow up in writing.

The Chair now recognizes the gentleman from Missouri, Mr. Cleaver, for 5 minutes.

Mr. CLEAVER. Thank you, Mr. Chairman.

Madam Chairman, last weekend, the Kansas City Royals lost a weekend series to the New York Yankees. Do you believe that the IRS was involved in any way?

[laughter]

Ms. WHITE. Do I believe what was involved? I am sorry.

Mr. CLEAVER. That is all right.

Ms. WHITE. It was pure skill by the Yankees, I think. I am from Kansas City, though, so I like them, too.

Mr. CLEAVER. Yes, I know you are. My real issue is regarding sequestration. Do you fear at all, or do you have any concern over the fact that with sequestration, that you will have the dollars to sufficiently oversee things such as the over-the-counter derivatives and a lot of other areas that this committee is going to hold the SEC responsible for monitoring and providing oversight?

Ms. WHITE. There is no question that the sequestration has an impact in that particular space, some of the hiring we need to do

to build out. And that was not a regulated market, or sets of market. It is a big one. It is a complicated one.

We are not able to—because of sequestration, that hiring can't occur now at least. And so, that is a concern.

Mr. CLEAVER. Let me stay with sequestration for a minute. Your predecessor, Ms. Walter, in a speech sometime back at American University, was suggesting—she did not say—but was suggesting Elisse—is that right? How do you pronounce the name?

Ms. WHITE. "Elisse."

Mr. CLEAVER. "Elisse"—that the SEC either wanted or had secured or was looking at some kind of technology that would allow you to study the markets quantitatively. Is that a reality now, or—

Ms. WHITE. I believe what she was referring to was the Midas system, which we are very excited about. And it will provide a lot of very useful information to the staff and the Commission on market structure. That is part of what our trading and markets group is analyzing, and including data from that informing the study we are doing of the equity market structure.

Mr. CLEAVER. Mr. Chairman, I yield back the balance of my time.

Chairman HENSARLING. The gentleman yields back the balance of his time.

The Chair now recognizes the gentleman from North Carolina, Mr. McHenry, for 5 minutes.

Mr. MCHENRY. Thank you, Mr. Chairman.

There have been comments about the IRS in this hearing. And some are trying to make light of what is a rather serious breach, and has a huge chilling effect on average Americans, average, everyday nonpolitical Americans. And it is a very serious matter.

Chairman White, thank you for your testimony. I know you have a very serious approach from your time as a U.S. Attorney, and you have carried that through now with your tenure at the SEC.

I have said publicly, and I have said to you, I have very high hopes for your tenure at a very troubled agency, a troubled agency on the enforcement front, which you are front-and-center on. And we, again, have high hopes for how you are going to follow the rule of law, and ensure that the agency adheres to that.

Likewise, we have some very important congressionally mandated rules. And I have expressed this to you directly as well. The JOBS Act was a bipartisan bill passed over a year ago and signed, one of the rare bipartisan bills that Congress was able to get through both the House and the Senate, and have the President sign.

We talked about enthusiasm. You have mentioned enthusiasm for the JOBS Act. It is about getting capital to small businesses and moderate-sized businesses, and get to that other function of the SEC, which is to foster capital formation.

So I ask you, Chairman White, where is the implementation? First, who sets the agenda at the Securities and Exchange Commission?

Ms. WHITE. I am told I do. So I am—

Mr. MCHENRY. Fantastic. Where is the JOBS Act implementation on your agenda?

Ms. WHITE. The answer is that it could not be a higher priority with me. I know you are looking for a time. It will be done as quickly as possible.

What I have done since I have arrived is to look at the work streams that were there, to make them more efficient and not overlapping, if I could, so that you didn't have the same people working on the same rules.

They remain, along with the Dodd-Frank rulemaking that isn't finished, at the top of my priority list. And I am going to get them done—I am on a 5-person Commission, even though I set the agenda—as promptly as I can.

Mr. MCHENRY. I respect that. We, on this side of the aisle, like the Commission's structure. But you set the agenda. I would like to know if Reg D, lifting the ban on general solicitation, is at the top of your agenda that you are setting?

Ms. WHITE. Certainly, I consider it to be the top. If we are saying there is one thing at the top, it is among the top things on my agenda.

Mr. MCHENRY. What is higher?

Ms. WHITE. There is nothing higher. I am proceeding on—as I said I would try to do—parallel tracks, depending on the readiness to go forward.

Mr. MCHENRY. We welcomed your announcement yesterday of a new Director of Corporation Finance, a permanent Director for Corporation Finance. You are reloading the staff there, and we encourage you to do that. That is where the JOBS Act regulations will be written.

On Section 2, I have asked about that. On an enhanced Reg A, we passed a bill yesterday with wide bipartisan support in the House to direct the SEC to get an enhanced Reg A-plus done by October 31st. Do you foresee being able to achieve that?

Ms. WHITE. Certainly, we will do everything in our power to do that. There is not a rule proposed yet. As you know, almost always, we have, for good reason, a notice-and-comment process.

I think it is a challenging date to actually have it done. Again, we are extremely focused on it. There are issues beyond just raising the amount that we need to be dealing with and are dealing with.

Mr. MCHENRY. This has been a long time coming. We had one offering in 2011 under Reg A. There has been a complete abandonment, and no serious review of Reg A within the SEC. And it is high time. That is why we mandated it within the JOBS Act.

Let us move to the crowdfunding. Where is crowdfunding on your agenda? That is a personal interest of mine, because that is a legislative priority that I have, and continue to have. And I want to see this capital flourish so we can get small businesses access to this capital.

Ms. WHITE. It is among those at the top. Nothing is higher in the sense that—I have several things at the top, and we are very focused on that. That is one where I know there has been both disappointment, and still excitement to get it done. So it is a very high priority to get it done as promptly as I can.

Mr. McHENRY. I urge you to set the agenda, to drive this train forward, and to make sure that we have full implementation of the JOBS Act. Thank you for your testimony.

Chairman HENSARLING. The gentleman yields back his 3 seconds.

The Chair now recognizes the gentlelady from Wisconsin, Ms. Moore.

Ms. MOORE. Thank you so much, Mr. Chairman.

And let me join my other colleagues in congratulating you on your appointment. Your outstanding credentials precede you. And hopefully, it will ploy you in these hard times.

Many on this committee, on both sides of the aisle, have asked you about your budget and about the sequester. So, I can't resist sort of pursuing that a little bit further.

You seem to be a little bit reluctant to give us the—to discourage us about it. But I am very concerned, as some folks are, about how you will actually be able to carry out the new mandates under Dodd-Frank with the—not only the sequester, but operating under the current continuing resolution. And even though there are no taxpayer funds that are at risk here, you still are subject to the sequester.

I think my colleague Mr. Green, in particular, laid out some of the challenges of oversight with regard to over-the-counter derivatives. But I am really curious about the amount of dark pooled trading that has occurred in the past couple of years. It has more than doubled.

And so, I am wondering about your ability to have oversight over that. Also, the push for having the so-called office of investor advocate and the accredited investors—how we will provide the adequate oversight of an area like that?

Ms. WHITE. Let me correct a misimpression. I am not shy about what we need. I don't mean to be. I was asking—I think, answering a specific question about sequestration and what the specific impacts—

Ms. MOORE. Right.

Ms. WHITE. —of that are on us.

We very much need what the President has asked for in this budget for Fiscal Year 2014. Again, the massiveness of our responsibilities is what sort of hit me between the eyes in the last month. And I am very concerned that if we don't get that appropriation, we cannot do our job. So, I don't want to be lacking in clarity there.

In terms of the market structure issue and the dark pools, again, that is one of the issues—that set of issues, the market structure issues—that, as I was being briefed to come onto this job, struck me as one to which we must bring a sense of urgency to fully understand all those issues so that we can regulate wisely in that space.

The data that is out there now is not conclusive—for example, high frequency traders have a speed advantage. But what the experts don't agree on is what the impact or harmful impact of that may be.

So, that is an area where I am also concerned about getting more market expertise into the mix at the SEC. And certainly, if we don't get the funding that we are seeking, that could be compromised.

Ms. MOORE. Thank you for that answer, for your candor.

We have been visited, I think, by companies that have indicated that they want to see—permit larger kick sizes for small companies in order to support secondary market research and market making. And, it makes sense in one sense. But I am wondering if the sequester and the C.R. are prohibiting the agency from studying that and moving that further.

It is the same thing with really giving us the definition of an accredited investor. I don't see Representative Stivers in here today, and we just sent you a letter May 10th regarding publishing your final rules on municipal advisers. I know there is a lot on your plate.

I was encouraged by your public remarks regarding the money market mutual funds, which kind of got politicized or something with the last Administration. So, I know I am asking a lot, but can you just tell me some of these things that are right on the precipice of being put out, what the time table is, what we can do here in Congress to help roll these things out a little bit faster?

Ms. WHITE. I appreciate the support, both in terms of our budget request and otherwise. Very much so. I think I have said publicly that I do expect in the near future on the further money market reforms, that will be keyed up by the staff for the Commissioners.

I have—again, my highest priority is the other rulemakings to finish on—in terms of the spread, the tick sizes. That was the subject of our roundtable recently. I think it was in February.

Under active discussion, we are sort of looking at whether there should be one or more pilot programs in order to further that, and that decision ought to be made pretty quickly, I think.

Accredited investors—we are very focused on that, as well, in terms of what should be done there. Clearly, we try not to have any of our core mission compromised by budgetary concerns, but it is not realistic to say that they are not.

Chairman HENSARLING. The time of the gentlelady has expired.

Ms. MOORE. I thank the chairman.

Chairman HENSARLING. The Chair now recognizes the gentleman from Michigan, Mr. Huizenga, for 5 minutes.

Mr. HUIZENGA. Thank you, Mr. Chairman. I appreciate that.

And Madam Chairman, I appreciate you being here, as well.

Neither one of us were around this institution when Dodd-Frank came into effect. But we are both dealing with the echo effects of it. And I want to explore that a little bit.

I have to tell you, I was thrilled earlier, I think, in one of your responses to my colleague, Mr. Neugebauer, from Texas. You said—I believe the quote was, it is one of your highest priorities to "simplify reporting requirements."

We have one of those solutions for you, myself and my colleague, Mr. Garrett from New Jersey. It is called H.R. 1135. It is dealing with pay ratio. And Section 953 of Dodd-Frank has been labeled by some a logistical nightmare because of all the different factors that are having to be put in place to consider calculating total compensation.

And I am curious—there are a lot of questions out there on whether transit benefits or employee-paid health care costs should be a component of compensation. Should domestic and all multi-

national employees be a part of the calculation? And what about part-time employees or independent contractors?

It seems to me that it is a vague statue, if you would agree or disagree with that. And what factors do you believe must be considered in determining this calculation? Have you looked at that at all?

Ms. WHITE. I have looked at that. And there are others who think very strongly that needs to be done as quickly as possible. The complication with that is in the definition of "total compensation."

And there is a specific definition of that which applies to when you are disclosing your top executive's compensation. That is, the statutory definition that leads to all the other issues you have just teed up in terms of some of those complexities.

Mr. HUIZENGA. I guess, ultimately, my question is, to what end? To what good? And that—when they sent around executive compensation and surveyed, they believe that is an estimate of 3 months—in some cases longer—to calculate and gather all those pay ratios.

And I am—I would love to know whether the Commission has—the staff has made any effort to identify the costs to business for this, when there is, in my view of it, absolutely no benefit to the health and well-being and safety and soundness of either a corporation or the investors in it.

It seems to me that it is trying to turn it into a political football. And I am curious—and we can—love to submit these, as well, to get maybe a further, more full answer from you. But it seems to me, we need to find out from you whether you believe that the significant amounts of time and money that are going to be spent developing it are worthwhile.

Ms. WHITE. Very quickly. It is a mandated rulemaking for us. So, as a regulator—

Mr. HUIZENGA. H.R. 1135 will take care of that. And we will alleviate you of that burden, so—the other thing I have is—we are working on some draft legislation regarding mergers and acquisitions, and earlier, you were talking about small businesses and trying to focus and concentrate on that.

Our proposal is to right-size Federal regulation of M&A intermediaries and business brokers. And it has been one of the top recommendations for the Government Industry Forum on Small Business Capital Formation, which the SEC annually holds. It has been a recommendation in 2005, 2006, 2007, 2008, 2009, 2010, and 2011.

Do you see that this is an important small business capital formation concern? And under your leadership, what priority are you going to be giving to these small business issues?

Ms. WHITE. I certainly appreciate the concern of that issue. And I will give a very high priority to small business issues during my tenure.

Mr. HUIZENGA. Okay. Just to clarify right now, presently, broker-dealer registration is a one-size-fits-all approach. And 90 percent of the requirements are totally irrelevant to a broker-dealer engaging in a limited capital raising activities. This could be something as small as selling an LLC. Because it has membership shares and those kinds of things.

And—

Ms. WHITE. I will commit to reviewing that specifically.

Mr. HUIZENGA. —that is great, because I know staff has acknowledged that concern, but the SEC has not addressed it yet. And I look forward to that.

Finally, on brokers, I just wanted to echo my friend, Mr. Meeks, as well. It seems that the SEC and the DOL are in a race. And one of those, in my opinion, shouldn't be in the race. It seems to me that we need to make sure that we are looking at that standard of care for retail accounts, especially when it is including those IRAs. And I am looking forward to an update from you on that.

So, those are my three issues.

Other than the last 10 seconds I have, we are talking budgets. According to my calculations, about $550 million of your budget goes to folks who make $100,000 or more on your staff. And I understand $100,000 in Washington, D.C., isn't the same as in Zeeland, Michigan. But you have 85.75 percent of your employees making $100,000 or more.

I would like you to review that, as well.

Ms. WHITE. We do need the expertise, too, though.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Delaware, Mr. Carney, for 5 minutes.

Mr. CARNEY. Thank you, Mr. Chairman.

And thank you, Madam Chairman—if that is the appropriate title—for coming in today.

Welcome.

You sound like you are just what the doctor ordered for this position. And we wish you well.

I don't think there is any risk that you are going to be bullied by anyone, as has been alluded to earlier. Anyone who has gone toe-to-toe with John Gotti and some of the folks that you prosecuted, I think we don't have to worry about being bullied.

I think a greater concern is that we will distract you from your priorities here in Congress, or not give you the resources that you need to do the job.

I support the request that you are making for your budget, as many of us here do. I hope, as our chairman emeritus said earlier, that we can come up with a bipartisan agreement on that.

Your expenditures are covered by the fees charged, and so it doesn't add to the budget, as you say, and we ought to give you the resources you need to—we can't afford not to, frankly, as has been stated by so many others.

Ms. WHITE. Thank you for that.

Mr. CARNEY. I would like to hear your opinion of H.R. 1256, the Swap Jurisdiction Certainty Act. I was a co-sponsor of that piece of legislation. The SEC came out with a proposed regulation, and in some ways, it mirrors the approach.

Could you tell us a little bit about your thinking there? You addressed it a little bit with Mr. Royce and Mr. Garrett earlier today, but tell me about your thinking and the prospects for getting that done in these various markets.

Ms. WHITE. The cross-border aspect as well?

Mr. CARNEY. Yes.

Ms. WHITE. Yes. It is a complex area. You obviously have a lot of regulators in the space in terms of—many of our proposals are consistent with our domestic counterpart the CFTC. We are working with them and the international regulators.

Mr. CARNEY. You are working with them right now?

Ms. WHITE. Yes.

Mr. CARNEY. So your hope is that you can have, as the legislation will require, a set of joint regulations. It doesn't make sense to us, I think, and I would be interested on your opinion, to have conflicting or different regulations there.

Ms. WHITE. I think the products are somewhat different between SWAPs and security-based SWAPs, so there can be differences, but clearly consistently is the objective—

Mr. CARNEY. Right.

Ms. WHITE. It is a very global marketplace. I believe that in your bill, H.R. 1256, there is a presumption that the top nine—

Mr. CARNEY. G8 plus Hong Kong is what it was.

Ms. WHITE. Yes. That is the only aspect that actually—not actually the only aspect, but that gives me some concern because I think what we have proposed is that the SEC make a judgment when requested about substituted compliance.

Mr. CARNEY. Right.

Ms. WHITE. Some of these countries really don't have regulations in that space so if we have to kind of—when it comes out of the gate, we have to basically prove that the presumption doesn't apply, it takes a lot of resources but—

Mr. CARNEY. But what should be clear is that you have the authority in the bill, and I would encourage you to use it. If those regulations are not what they ought to be from your perspective, then you can apply the SEC's regulations to those U.S. companies, U.S. persons as defined—

Ms. WHITE. I think our staffs are working on this aspect.

Mr. CARNEY. Yes.

Ms. WHITE. So, okay.

Mr. CARNEY. That is great. I think it is important that it get done that way, certainly that there is consistently and I think, as has been referenced earlier by others, the confusion and lack of clarity can create more problems than if you have a consistency there.

So that is really all I have. I want to, again, welcome you. Thank you for your willingness to take on this very important position. I hope, after today's hearing, you don't have second thoughts and decide to do something else.

Ms. WHITE. I haven't left the room yet, at least.

Mr. CARNEY. No, you haven't. You haven't left the room. You are still here and we wish you well. Thank you.

Ms. WHITE. Thank you very much.

Chairman HENSARLING. Nor are you allowed to for another 45 minutes.

Ms. WHITE. I know that.

[laughter]

I knew that.

Chairman HENSARLING. The gentleman yields back.

The Chair now recognizes the gentleman from Virginia, Mr. Hurt, for 5 minutes.

Mr. HURT. Thank you, Mr. Chairman.

And let me, again, echo my thanks for your being here. As a former prosecutor, I especially appreciate your history and experience in enforcement of the laws of the United States.

I certainly think that we would all agree that the firm and fair enforcement of the laws is very important to cultivating our capital markets and instilling confidence in them.

I would also echo what has been said about the importance of implementing the JOBS Act. I come from a rural district in Virginia where we have places with unemployment at 10 percent, some places have been up to as high as 20 percent.

We need jobs, and I believe capital formation will lead to that. One of the things that, in additional to enforcement, or one of thing—one of the responsibilities, in addition to enforcement, obviously is facilitating capital formation.

It would seem to me that when you have 4,000 employees, and you look at the breakdown of economists versus lawyers, you have 59 economists, and you have 1,750 lawyers, I guess the question is, how do you facilitate capital markets when you have that ratio of enforcement versus market expertise that Mr. Royce talked about?

Ms. WHITE. I think first, we are, as you noted, a law enforcement agency and so certainly we have a significant number of lawyers in our enforcement division and our examination divisions to enforce the laws and to look for compliance in the laws.

But in terms of the economists that we have, we do have 59. Now, one of our requests in this budget request is for another 45 positions, I think 10 of them would actually be Ph.D. economists, but all have expertise—I don't know if they are all nonlawyers, but close to that for our risk strategy and financial innovation division, which is where we do that kind of analysis.

We have experts elsewhere in the other divisions, too, particularly in enforcement now. We will always need to have a very significant complement of lawyers, but where you have seen the most growth, including this budget, is in the arena of the economists and experts to support them.

So you have to get the right balance there, but a big part of what we do is law enforcement and that is going to lead to a lot of lawyers.

Mr. HURT. Thank you. With respect to the health of the capital markets in the United States, one has been offered that the best measure of that is, in fact, the number of IPOs that we see on an annual basis.

We know that number had declined. In fact, the reason that we adopted the JOBS Act was to try to encourage more of that activity and try to take the burdens that we in Washington place on that activity, try to take them away at least temporarily.

I wish we could do it permanently, but we have recognized, as a body, that we need to do that at least temporarily to help encourage this.

It is particularly discouraging that those numbers wane when you consider the number of IPOs that you see in other countries. And so, I was wondering if you could speak to that? Does that con-

cern you? And what specifically can we do in Washington to encourage more of that activity?

Ms. WHITE. I guess one just sort of data point, although I don't want to overstate this, is there has actually been an uptick in IPOs and the value of IPOs in this first quarter or so of this year.

It doesn't mean that it lasts. Obviously, it is a matter of real concern. I think I mentioned before the capital formation study that the Corporation Finance Division in the SEC was doing before the JOBS Act was enacted; was partially directed at that.

I think it is a complex set of factors. It is not easy to sort of say this will do it, but it is certainly something we are very focused on studying and to make a contribution to that analysis as to whether further legislation might help it, other things might help it—

Mr. HURT. And wouldn't you agree that those diminished numbers must be, at least in some part, a reflection of the policies that are adopted at the SEC and here in the United States Congress?

Ms. WHITE. You certainly focus on whether that is so, particularly for smaller businesses. But I think it is a very complex subject, so I don't have an answer for you on that, but you certainly focus on the question quite closely.

Mr. HURT. Thank you. I yield back my time.

Chairman HENSARLING. The gentleman yields back. Mrs. Beatty from Ohio is recognized for 5 minutes.

Mrs. BEATTY. Thank you, Chairman Hensarling, and Ranking Member Waters.

And thank you, Madam Chairman, for being here, and I certainly join my colleagues in thanking you for sitting through all of this today. And certainly, as you stated in your testimony, the breadth of what you do there is vast.

With that said, I have two questions. One, being an OMWI, I guess I could say, person because I am a minority and a female and being a small business owner, last month the SEC's Office of Minority and Women Inclusion submitted their annual report.

And in the report, it talked about the percentage of contracts that went either to women or minorities and while there was a small increase, 21 percent, I believe, of the contracts went to either a minority or a female.

But when they separated them and looked at them, there was a decrease in contracts going to minorities. I get a lot of questions, because I have been a small business owner for over 20 years, from people who are female or minorities wanting to know with the Federal Government and, more specifically, with the SEC, how they can get engaged.

So I guess my question to you is, can you discuss briefly how you would approach increasing the participation of minorities and women doing business with the Commission?

Ms. WHITE. Yes, and we are very focused on that, as is the head of our OMWI office. Part of what we are doing, and it will be enhanced as we go forward, is a lot of outreach to potential vendors and contractors with the SEC.

So you can at least make the process clear? Is it available? How do you participate in that process? Actually, we were pleased with the results of those efforts so far, but we have obviously much further to go.

But we are quite focused on—the outreach has been—efforts and they have been extensive and a lot of them and I think giving really clear instructions as to how best to compete for those contracts.

But we need to do more in that space, no question.

Mrs. BEATTY. Okay, and my second question is, in 1982, an accredited investor was required to have at least a million dollars or $200,000 in cash.

So here we are, 30-some years later, after inflation has cut the value of a dollar by almost two-thirds. Do you think an individual still should qualify as an accredited investor with those same dollar amounts?

Ms. WHITE. I think that is an issue, and I believe my predecessor actually testified before a subcommittee or this committee about it, which we are very focused on at the SEC and really considering what the range of factors should be. Not just the dollar amounts, but what else should go into an optimal definition of accredited investor as we sit here in 2013. So, that is being worked on.

Mrs. BEATTY. Thank you. I yield back the rest of my time.

Chairman HENSARLING. The gentlelady yields back.

I now recognize the gentleman from South Carolina, Mr. Mulvaney.

Mr. MULVANEY. Thank you.

Madam Chairman, I want to focus on my questions or at least with my questions on the SEC's mandate, which I have as to protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation.

So on the facilitate capital formation, let us talk a little bit about the budget request that you bring to us for 2014, $1.674 billion, which by the way, I think, if my math is correct, represents about a 26 percent increase over the 2012 budget.

And I guess, as a point of departure, is it fair to say your workload has gone up by 26 percent in the last 2 years? What is driving that? That is a fairly dramatic increase in a time when most folks are looking at reductions in their budgets. So, tell me a little bit about that.

Ms. WHITE. Okay. To start with that, I think it is—we obviously have new responsibilities we have talked about under Dodd-Frank, significant new responsibilities.

Mr. MULVANEY. Right. But Dodd-Frank was before 2012.

Ms. WHITE. Yes. But the build-out of what you need—the regulations are still under consideration being proposed. The personnel that you need, and the structure that you need is basically coming now in order to build that. So, that is a part of it.

I think the other part of it is—and part of our request, by the way, does go for additional positions in Corporation Finance, for example, which is dealing with the implementation of the JOBS Act, the amendments.

Some of it is that we just haven't had the funding in the past to do our job. And I can't really say it any other way.

Mr. MULVANEY. This comes out of the fees paid by folks who are using the services. Would you agree with me that every penny that goes to the SEC for its budget is money that is not available for capital formation?

Ms. WHITE. I wouldn't agree with that, actually, no. Because I think what we are focused on with really everything we do, including—in my mind, they don't sort of separate out investor protection, orderly and efficient markets, and capital formation.

So when we essentially fund something that goes, let us say, predominantly to investor protection, as some people would see it, that also facilitates capital formation. So I don't see that as a—

Mr. MULVANEY. So is it fair to say it is not available for capital formation? When you take it, you take it out of the market, and it is no longer available for capital formation?

Ms. WHITE. I would agree. I think it is $0.02 to $1,000.

Mr. MULVANEY. Let us talk about the other portions of the mandate—protecting investors, and orderly and efficient markets. Help me understand which of those three mandates speaks to the conflict minerals rule.

Ms. WHITE. The conflict minerals rule is a congressionally mandated rulemaking. We obviously went through our process.

Mr. MULVANEY. Is it fair to say that it doesn't—that none of the three mandates really speak directly to the conflict minerals rule? It may be our fault, and that is blaming you. But—

Ms. WHITE. No, no. I appreciate that. I have heard arguments that it advances one or more of our tripartite mission. But I take your point.

Mr. MULVANEY. Is it fair to say that perhaps it is possible that other rules may be more in line with your mandate than the conflict minerals rule?

Ms. WHITE. It is under litigation. Certainly, part of our mandate is to do the rulemaking that is required of us by Congress.

Mr. MULVANEY. Okay. Let us talk about that. Because you are right, and I can't disagree with that, because it is the law. But my point is that it looks like—and I know I am not alone in this—there are other rules from Dodd-Frank, so ones that are contemporaneous with the conflict minerals rule, that don't have rules yet, that are either late or haven't even started yet.

In fact, I think that Commissioner Gallagher, in his speech back in September, gave a perfect example. He said, "The mandate in Dodd-Frank, Section 939(a) for Federal agencies to remove references to credit ratings from the rule books may well be the clearest, most direct mandate we at the SEC have been given. It has the virtue of being responsive to one of the core problems underlying the financial crisis."

Yet, that rule went after—it is not even finished yet, I don't think—conflict minerals. Why is that? Why did the conflict minerals go before other rules that apparently at least one of your Commissioners thinks are much more in line with your mandate?

Ms. WHITE. At least as I see my space, there are a lot of mandated—there are lots of mandates that are quite clear from Congress.

That is one where we have moved forward on some of our regulations and statutes. There are also discussions among the staff and the Commissioners on others. Again, I go back to—

Mr. MULVANEY. Do you know why conflict minerals 1502, 1504, went before 939(a)?

Ms. WHITE. I don't know that. It precedes my time there. So I don't know. It is in a different division than the credit rating issues and rules. But I am not saying that is the explanation for it.

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

Chairman HENSARLING. The gentleman from Washington, Mr. Heck, is now recognized for 5 minutes.

Mr. HECK. Thank you, Mr. Chairman.

Chairman White, let me add my voice of congratulations, not just for your nomination, but for your successful confirmation.

I have a couple of quick questions regarding H.R. 1062, if I may, please. We have discussed that briefly here this morning. To begin with, in your opinion, and with advanced apologies for my split infinitive, in your opinion, is passage of H.R. 1062 necessary in order for the SEC to successfully fulfill its statutory mission?

Ms. WHITE. I certainly—is it necessary to pass it to do that? Is that the question? I'm sorry. I didn't quite catch your question.

Mr. HECK. Is passage of H.R. 1062 necessary in order for the SEC to successfully fulfill its statutory mission?

Ms. WHITE. I do not believe so. I am a firm believer in robust economic analysis, which is very much a part of our mission, and requirements that we assume, and that inform all of our rulemaking.

But I am concerned that H.R. 1062 would layer on additional and different requirements that are not obviously presently required by law, and not necessary to our robust rulemaking. And I would worry that we couldn't carry out our mission as we do now.

Mr. HECK. In that regard, would you then therefore characterize it as undesirable in your pursuit to successfully fulfill your statutory mission?

Ms. WHITE. I certainly would be very concerned about whether we could do our job if it passed.

Mr. HECK. Lastly, given your reference to your avowed allegiance to robust economic analysis, including cost/benefit analysis, in your opinion, has the level of recent economic analysis, cost/benefit—presumably, including cost/benefit analysis by the SEC, been a material factor in impeding or inhibiting the facilitation of capital formation in the marketplace?

Ms. WHITE. The answer is, I think it is essential to good rulemaking. Let me just be very clear about that. Obviously, it takes time and resources, as do a lot of things that are difficult but important do.

So I do think we need, at the agency, to be able to carry out that robust economic analysis to which I am firmly committed in a way that it doesn't impede our ability to promptly carry out our rulemaking mandates.

Mr. HECK. I am not sure I understood how your answer was responsive to my question. So—

Ms. WHITE. I apologize.

Mr. HECK. Let me ask again. In your opinion, has the recent level of economic analysis by the SEC been a material factor in impeding or inhibiting the facilitation of capital formation in the marketplace?

Ms. WHITE. I don't think—and I am not trying to be nonresponsive—I can answer that other than to say that all the work we do

that takes time can obviously slow down a rulemaking that may facilitate capital formation.

But I wouldn't single out economic analysis for that. And I do think it is very important to informing wise rulemaking.

Mr. HECK. I was trying to be as objective as possible by asking it in terms of, at the level. But let me ask with kind of a more biased characterization.

Has the absence of robust economic analysis and cost/benefit analysis been a material factor in impeding or inhibiting the facilitation of capital formation?

Ms. WHITE. I don't think at the SEC there is an absence of robust economic analysis. I do not think—

Mr. HECK. Including cost/benefit analysis?

Ms. WHITE. Including cost/benefit analysis. And I think third parties have made that observation recently that we are doing a very good job at it.

Mr. HECK. Is there any way I can reasonably or logically infer from your comments, other than that your view is H.R. 1062 is both unnecessary and undesirable?

Ms. WHITE. I am troubled by H.R. 1062 for the reasons I have stated.

Mr. HECK. Thank you, Madam Chairman.

I yield back the balance of my time, Mr. Chairman.

Chairman HENSARLING. The gentleman yields back.

Mr. Hultgren is recognized for 5 minutes.

Mr. HULTGREN. Thank you, Mr. Chairman.

Chairman White, thank you so much for being here. I appreciate it, and I appreciate your service.

I have a couple of questions for you. The agency that you now lead has had some challenges and some failures in the past years: it failed to prevent a taxpayer bailout of Bear Stearns; it failed to prevent the collapse of Lehman Brothers; it failed to do anything about the largest investment banks loading up on toxic assets; it failed to transfer employees to the now defunct Consolidated Supervised Entities Program, which oversaw the five independent investment banks, two of which failed spectacularly during the financial crisis; it failed to do anything about the credit rating agency oligopoly that bestowed AAA ratings on securities that later proved to be no better than junk; and it failed to uncover two multi-billion-dollar Ponzi schemes run by Allen Stanford and Bernie Madoff, despite multiple warnings by market professionals, resulting in untold economic harm to thousands of individual investors.

Also, your agency has received a 300 percent increase in the last decade in your budget. Your agency has missed 70 percent of Dodd-Frank rules and 100 percent of JOBS Act rules.

With all of those failures, why should you and the SEC be rewarded with a $1.674 billion budget?

Ms. WHITE. I think the agency would not dispute that it has had challenges, and had some of the issues that you have identified. I think the SEC, before my arrival, has also done a great deal to remediate those issues.

I think we have to—when we step back and look at sort of percentages of budget request increases, you also have to look at, so what are the responsibilities, what is the market that we regulate?

And you have had an—obviously, a vast growth in the equities market. You have had a vast growth in the SEC's responsibilities to regulate. Assets under management have more than tripled.

So I think if you sort of laid those side by side, those budget increases would make very good sense, but in my judgment, would not be sufficient for us to carry out what is on our plate today to fulfill our missions, including the congressionally mandated rule-making, but really, all of our responsibilities over this marketplace. We have tried to pinpoint exactly what we need, and say why.

Mr. HULTGREN. I think that gets to some of the concerns I have heard from my colleagues as well, that with all these failures, and then with rules congressionally mandated activities that are being pushed off to do optional activities concerns us when there is a request for additional dollars.

Let me shift gears, because I just have a short time. But Chairman White, I wonder if you could discuss the economic and cost/benefit analysis that FINRA is required to perform when it issues a new rule, a rule amendment, or an interpretation? And how does the SEC oversee that process?

Ms. WHITE. I think in terms of the SROs, they are not subject to the SEC guidance, per se, in terms of economic analysis and cost/benefit. The rules are put out for public comment. Often, the comments include comments about cost and cost benefits.

The SEC, in its oversight role of the SROs, makes certain that those comments are taken into consideration. When we get a rule-making from the SROs, for example, they do provide what they think the impact will be of their rules.

Mr. HULTGREN. Let me ask you this, does FINRA also consider cost/benefit and economic issues when administering its other operations, such as its exam and inspection programs?

Ms. WHITE. The answer is even as a formal matter, as a formal matter do they? I don't know the answer to that. I think they certainly do in a—I don't want to use the word "holistic" again, but I guess in a holistic sense. I may need to get back to you on that—

Mr. HULTGREN. If you could, that would be great. If you can give us some more information on it for the record, that would be terrific.

[Additional information provided by Chairman White can be found on page 110 of the appendix.]

Mr. HULTGREN. Mandatory arbitration is hardwired in definitive rules. It compels broker-dealers to arbitrate disputes if the customer elects. If and when the SEC reviews whether broker-dealership had the same right to include arbitration clauses in their customer contracts, do you agree that customers and broker-dealers are entitled to fair and equal treatment with respect to mandatory arbitration, whether it is imposed through FINRA rules or by agreement of the parties in the customer contract?

Ms. WHITE. Certainly, to be fair and equal treatment, in terms of mandatory pre-dispute arbitration, I talked about that a little bit earlier, that the SEC has been given authority to deal with that, hasn't made a decision what, if anything, should be done about it.

Mr. HULTGREN. In my last remaining seconds, when does the SEC expect to finalize the risk retention rule mandated by Dodd-Frank?

Ms. WHITE. That is something that is preceding actively. That is one where we are required to do joint rulemaking with other regulators. So that is the process for that. But it is in quite active dialogue now, and is progressing.

Chairman HENSARLING. Time is—

Mr. HULTGREN. My hope is to finish up quickly.

I yield back, Mr. Chairman. Thank you.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair recognizes the gentleman from Arkansas, Mr. Cotton, for 5 minutes.

Mr. COTTON. Chairman White, thank you for your time today. Thank you for your distinguished service to our country and your willingness to come serve again.

I would like to talk a little about the potential for a political expenditure disclosure rule. Your spokesman, John Nester, said earlier this week that the timing of such a rulemaking "will be influenced by the ongoing workload of Dodd-Frank and JOBS Act rulemaking."

Can you tell us, where does the political expenditure disclosure rulemaking rank in SEC priorities?

Ms. WHITE. The status of that is that it is—the petitions we have received seeking that disclosure are being reviewed in the Division of Corporation Finance with a goal to determine whether or not to recommend the pursuit of any rulemaking.

There is no proposed rulemaking being worked on now. Finally, the Division of Corporation Finance has a lot of these rules, mandated rules we have been talking about. And so, that is all I can say about the status.

I haven't been given the results of that review. But no rule is being worked on.

Mr. COTTON. Would such a rulemaking ever precede rulemakings on the dozens of rulemakings that have missed deadlines from the Dodd-Frank Act or the JOBS Act?

Ms. WHITE. The answer is that the focus is on the congressionally mandated rulemakings. We have to be able to engage—not speaking about this one in particular—but with important discretionary rulemaking.

But the focus—again, I have said what the status of that is. The focus of Corporation Finance, which is the division that is reviewing these petitions, is on the mandated rulemakings.

Mr. COTTON. You have, I know, many fine staff attorneys who are experts in corporation finance regulations and laws. I attended school with some, served with some who were hired by your agency because of their expertise.

My legal skills were such that I left the law and joined the Army, and went to fight in Iraq and Afghanistan.

Ms. WHITE. Thank you for your service.

Mr. COTTON. Thank you. How many experts in the mishmash of campaign finance laws do you have at your agency?

Ms. WHITE. I don't know who might have specific expertise in that. Sometimes people have expertise you don't know about. But

obviously, you are familiar with kind of the profile of expertise that we have at the SEC and that we don't have at the SEC.

Mr. COTTON. Yes. There are very complicated laws, because oftentimes they are simply complicated, incumbent protection rackets that politicians in both parties who like to stay in office have passed.

Getting on to the substance of a potential rulemaking like that, would it apply to corporate spending only, or could it potentially reach the spending of directors and officers in their personal capacities as well?

Ms. WHITE. My understanding of what is being reviewed are the petitions. I think with the petitions have sought is the spending by the corporations. But I believe it is confined to that.

Mr. COTTON. Do you think it would be appropriate to require a publicly traded company to disclose the private political activities of its officers, directors, or other employees and agents?

Ms. WHITE. Because that is at least part of the subject matter that is under review, not the precise subject matter, I don't think I should comment or prejudge until I have the benefit of the staff's review.

Mr. COTTON. If you proceeded with the rulemaking, would that rulemaking be applied to labor unions?

Ms. WHITE. I don't want to speculate. Specific petitions are being reviewed. There is no recommendation. No one has reached a conclusion as to whether there should be any proposed rulemaking going forward. But I certainly can't talk about the dimensions of something that hasn't proceeded out of the review stage.

Mr. COTTON. Do labor unions file any reports with your agency?

Ms. WHITE. Specifically, not that I am aware of.

Mr. COTTON. Me, either. I must have been confused when I asked that question. They file reports with the Department of Labor, fill a form LM-1, 2, 3 and 4. Are you aware of any efforts by the Department of Labor to impose similar requirements on labor unions?

Ms. WHITE. I am not.

Mr. COTTON. Would any rulemaking by your agency apply to nonprofit organizations such as MoveOn.org, or Organizing for America?

Ms. WHITE. I can't comment on what dimensions of something that I don't have the benefit of the review or any recommendation whether or not to proceed with any proposed rule.

Mr. COTTON. I would assume that such a rulemaking would not apply to such nonprofits, since those are normally regulated by the Internal Revenue Service.

Final question, are you concerned at all about partisans of the President and the left using your independent agency to help develop a political-enemies list of the President?

Ms. WHITE. I am not. I think the SEC is an independent agency, and I am a very independent chairman of that agency.

Mr. COTTON. Yes, ma'am, you are, and I appreciate your service.

Chairman HENSARLING. The time of the gentleman has expired.

The Chair now recognizes the gentleman from Pennsylvania, Mr. Rothfus, for 5 minutes.

Mr. ROTHFUS. Thank you, Mr. Chairman.

And again, let me echo Representative Cotton's commendation on your service, the distinguished career you have had in the prosecutions of terror in New York City. So, thank you for that.

If I can just follow up a little bit on the disclosure of the political contributions rule, just an issue that occurs to me is, how far-reaching might this be, as your staff looks at that? For example, municipal bonds, we have issuers across the country, school boards or school districts issuing bonds. Are we going to get into the political contributions of school directors?

Are we going to get into the political contributions of hospital administrators, as a hospital—the municipal bond market? Again, we have no idea what the contemplation is, the frustration is, that this is a discretionary effort, while we are waiting for mandatory regulations under the JOBS Act. So, I will just ask you to comment on that.

Ms. WHITE. The highest priority is the congressionally mandated rulemakings. Again, what the staff is reviewing are petitions submitted to the SEC. Obviously, they don't—they seek what they seek, right, which is narrower than the concerns of the Chair. But I take your points.

Mr. ROTHFUS. Thank you. It seems to me that the only place in this country that is really booming is this town we are sitting in right here. And your arrival in Washington coincides with the tremendous growth of the wealth of this City.

It has the highest per capita income in the country. Seven of the 10 richest counties in the country are right around Washington, D.C. And it seems that the bigger this town gets, the more negative impact it has on the rest of the country.

In Fiscal Year 2010, when Congress and the White House were under unified Democrat control, and more than a year after the fiscal crisis that hit, the SEC's budget was $953 million. Four years later, the Administration is here looking for a $1.6 billion allocation. That is a 70 percent increase in just 4 years.

We need to have the right tax and regulatory policies in place to get the rest of the country booming again. And getting these regulatory policies right means we need to think about the impacts of regulations, the burdens on business. We really need that cost/benefit analysis.

How does the SEC measure the pros, and cons, and burdens, and benefits in its rulemakings?

Ms. WHITE. It is a very—I keep using the word, but it is a very robust process, where all those factors are taken into consideration. I think probably it was entered into the record the easiest place to sort of look at our process is to look at the guidance that was issued in March of 2012. But plainly, all of those impacts are considered.

Mr. ROTHFUS. We are competing with the rest of the world in capital formation. And we want to attract businesses to this country, to invest in this country, and to raise capital in this country so we can get jobs going in this country.

And it seems to me that we need to be cognizant of that marketplace, and making sure that our regulations aren't going to be driving businesses offshore.

Ms. WHITE. And I think those are obviously extremely important impacts.

Mr. ROTHFUS. Thank you. I yield back.

Chairman HENSARLING. The gentleman yields back.

The Chair recognizes recognizes the gentleman from Kentucky, Mr. Barr, for 5 minutes.

Mr. BARR. Thank you, Mr. Chairman.

Chairman White, thank you for your service. And congratulations on your appointment and confirmation.

I wanted to explore, and continue to explore the issue of coordination between your agency and the CFTC, particularly with respect to implementation of Title VII of Dodd-Frank. Mr. Garrett, Mr. Royce, and Mr. Carney, during this hearing, have highlighted the divergence of some of the rulemakings or proposed rulemakings between the SEC and the CFTC.

And an example of that is the cross-border application of derivative reforms, which has been very controversial, and potentially very disruptive. An example of this would be foreign regulators who have expressed concern, and even come to Congress to highlight the significant competitive disadvantage that U.S. actors would experience.

For example, Masamichi Kono, a Japanese regulator, asserted that, "There are firms outside the U.S. who have started to decline transactions with U.S. counterparties because of the uncertainties in the rules and also the apparent lack of coordination between regulators."

Likewise, Patrick Pearson, head of financial market infrastructure at the European Commission, concluded, "We produce for regulators an 80-page comparison between 342 pages of European rules and all of the relevant rules in Title VII and the CFTC requirements. The message is, we have a problem. That is an objective fact."

Now, I would commend the SEC and your deliberative approach on this issue, unlike the CFTC, the proposed rule and comment that you all—that procedure that you all have followed. And my question would be, why did you all choose this approach?

Could the deliberative approach alleviate the chaos around the CFTC's guidance of last October? And specifically, in reference to your response to Mr. Garrett when you said that you are committed to working with CFTC Chairman Gensler, can you address how you will deal with the need for coordination on this cross-border issue?

Ms. WHITE. Yes. First, I would say the Commission did unanimously propose the cross-border rule. We think it is a robust rule, but we also are cognizant of the global marketplace and other regulators in it.

We are very concerned about preventing risk to the United States from securities-based swaps transactions, wherever they occur. Our model is the substituted compliance model, which we think is a step forward that carries out the statutory objectives, but takes account of the global marketplace.

So we have gotten some positive feedback on that from our counterparts. We continue to discuss with the CFTC and our foreign regulators just how to do this best. Obviously, we have put out a

proposed rule. We had the benefit of comments that the CFTC got before on what they did.

We are continuing the dialogue. We will obviously take the comments that we get quite seriously. But I think what the regulators have to do in the United States and abroad is to solve it in an optimal way.

Mr. BARR. Specifically, in terms of your interface with Chairman Gensler, the CFTC has exemptive relief on cross-border that is, I think, slated to expire on July 12th. And as I understand it, that is in the middle of your own comment period on the issue. Is your preference that the CFTC continue the exemptive order to allow consistency or to provide for consistency?

Ms. WHITE. I think, ultimately, the objective here—even though it is not mandated—is consistency. Plainly—and we hear it everywhere—I am sure you hear it everywhere—market certainty is awfully important everywhere, but particularly in this space, it is a heretofore totally unregulated space, basically. That is one of the problems that was being dealt with in Title VII. So I think we should and we are in continuous dialogue to try to try to come to consistency.

Mr. BARR. Another example of perhaps divergence between SEC and other regulators, the SEC has proposed capital rules for nonbank security-based swap dealers that largely follow the capital rules for registered broker-dealers, even though these rules differ in significant ways from the capital rules for derivative dealers proposed by CFTC, my understanding is that the SEC's proposed capital rules for nonbank security-based swap dealers are generally more onerous than those that apply to CFTC-regulated swap dealers or banks that act as dealers, in particular because of the large capital deductions that apply only under the SEC's proposed rules.

Again, a competitiveness issue. Could you comment?

Ms. WHITE. I would probably have to get back to you on the details of that, but plainly, a focus as we go through this includes competitive impact, but I would probably need to respond to you further.

Mr. BARR. We can provide that in writing, and we appreciate your work to continue to facilitate coordination.

Chairman HENSARLING. The time of the gentleman has expired. There are no other Members in the queue. In recognition of Chairman White showing up early for the hearing, we will allow her to depart early from the hearing.

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.

Again, I want to thank the Chairman for her testimony today. This hearing is adjourned.

[Whereupon, at 12:53 p.m., the hearing was adjourned.]

A P P E N D I X

May 16, 2013

Statement of Randy Neugebauer
Full Committee Hearing
"Oversight of the SEC's Agenda, Operations, and FY14 Budget Request"
May 16, 2013

Thank you, Mr. Chairman, for holding this important hearing today. And thank you, Chair White, for testifying before the Committee. I am optimistic that under your leadership, the SEC will become more transparent, innovative, efficient and accountable.

At a time of unprecedented fiscal uncertainty, we need to rely on our agency heads to be good stewards of taxpayer money and reward those agencies that can demonstrate that they are using *existing* staff and technology as effectively as possible. With regard to the SEC, we are looking to you to run the Commission in a streamlined, efficient and business-like manner that protects investors and allows our businesses to successfully compete in the global marketplace.

The Washington narrative about the financial crisis and its aftermath is that it was somehow caused by a lack of regulation. But when you go back and look at a lot of the failures from a regulatory standpoint, the laws were on the books that would have prevented most of those events from happening. Whether it was Madoff, Stanford, failed oversight of Bear Sterns or Lehman, or the Reserve Primary Fund from "breaking the buck", the resources and regulations were in place to prevent these occurrences.

So it is not that we need more money for more regulations and more regulators; we simply need regulators who do their jobs and enforce the existing laws.

My fear is that in reaction to the financial crisis we have thrown this big blanket – called Dodd-Frank - over our capital markets. And as a result, we have created a new type a risk called "regulatory risk." And unfortunately, this new "regulatory risk" is making the United States a less attractive place to do business.

As much as some of my colleagues would like to make markets risk-free, I remind them that risk-free markets are opportunity-free. I look forward to hearing from Chair White on how she plans to reduce the "regulatory risk" that is impeding the development and competitiveness of our capital markets.

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Testimony on Oversight of the SEC
by
Chair Mary Jo White

Before the
U.S. House of Representatives Committee on Financial Services

May 16, 2013

Chairman Hensarling, Ranking Member Waters and Members of the Committee:

Thank you for the opportunity to testify on behalf of the Commission regarding the recent activities of the U.S. Securities and Exchange Commission (SEC). I have been Chair of the SEC for only a month, but in this short period of time I have been extremely impressed by the commitment, talent, and expertise of my fellow Commissioners and the agency's staff. The challenges before us are many, but I am confident that we will work tirelessly together in an effort to fulfill the broad, three-part mission of the SEC: to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation.

The breadth of the SEC's jurisdiction is vast – our Divisions and Offices are responsible for implementing and enforcing the federal securities laws, overseeing thousands of key participants in the securities markets (over 25,000 entities currently),[1] and reviewing disclosures and financial statements of more than 9,100 reporting companies. In recent years, the agency has made significant strides to strengthen its examination and enforcement functions, improve its capacity to assess risks, and enhance its technology, and also has made internal improvements designed to maximize efficiencies and reform its operations. Much more, however, remains to be accomplished.

With the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) and the Jumpstart Our Business Startups Act (JOBS Act), the agency's importance and scope of responsibilities are greater than ever, with the Dodd-Frank Act giving the Commission additional responsibilities for over-the-counter derivatives, hedge fund and other private fund advisers, municipal advisors, security-based swap clearing agencies, and the JOBS Act providing for several new or revised exemptions from the registration requirements of the Securities Act, including a new regime for crowdfunding offerings. Although the SEC has proposed or adopted rules for over 80 percent of the more than 90 Dodd-Frank Act provisions that require SEC rulemaking, there is much Dodd-Frank work that remains. Similarly, the JOBS Act requires significant Commission rulemaking which is not yet finalized. I believe that the SEC must complete, in as timely and smart a way as possible, the rulemaking mandates contained in both the Dodd-Frank Act and JOBS Act.

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[1] These participants include about 10,600 investment advisers, 9,700 mutual funds and exchange traded funds, 4,600 broker-dealers, and 460 transfer agents. We also oversee 17 national securities exchanges, eight active clearing agencies, and 10 nationally recognized statistical rating organizations (each, an NRSRO), as well as the Public Company Accounting Oversight Board (PCAOB), Financial Industry Regulatory Authority (FINRA), Municipal Securities Rulemaking Board (MSRB), and the Securities Investor Protection Corporation (SIPC), and the Financial Accounting Standards Board (FASB).

I also believe that the SEC needs to be in a position to provide expert oversight over today's highly complex and dispersed marketplace so that it can be wisely and optimally regulated. Such oversight must come without undue cost and without undermining market vitality. While this will entail additional investments in technology and expertise, the goal is to help the agency keep better pace with the markets we monitor and regulate while also permitting us to see around corners and anticipate issues that may arise.

Beyond this, I also feel that the Commission needs to further strengthen the enforcement and examination functions of the SEC. Strong enforcement of the securities laws is necessary for investor confidence and is essential to the integrity of our financial markets. Successful enforcement actions result in sanctions that deter and punish wrongdoing and protect investors, both now and in the future. Similarly, our National Examinations Program is critical to improving compliance by regulated entities, preventing and detecting fraud, and monitoring market risks.

My testimony today will highlight the work of each of the SEC's Divisions and many of its Offices, including the SEC's progress implementing the Dodd-Frank Act and JOBS Act. I also will briefly discuss the agency's FY 2014 budget request.[2]

Enforcement

A vigorous enforcement program is at the heart of the SEC's efforts to protect investors and promote the integrity of the marketplace. As the agency's largest division, the Enforcement Division (Enforcement) investigates and brings civil charges in federal district court or in administrative proceedings based on violations of the federal securities laws. Successful enforcement actions result in sanctions that deter wrongdoing, protect investors, and result in penalties and the disgorgement of ill-gotten gains that can be returned to harmed investors.

In FY 2012, Enforcement continued to perform at a high-level, utilizing its enhanced expertise and specialization capabilities to file tough enforcement actions that sent a strong deterrent message in an increasingly complex and global securities market. In the aftermath of the financial crisis, the SEC obtained orders requiring the payment of $3.1 billion in penalties and disgorgement in its filed enforcement actions in FY 2012, with a total of $5.9 billion in penalties and disgorgement in the past two years. The Commission does not, however, set quantitative targets for Enforcement activity, and quantitative metrics alone are not a complete yardstick of the measure of Enforcement's effectiveness. Consistent with Commission guidance, Enforcement considers the quality, breadth and effect of the actions pursued.

Enforcement's specialized units – Asset Management, Market Abuse, Structured and New Products, Foreign Corrupt Practices Act, and Municipal Securities – continue to build institutional knowledge and experience that allow our attorneys to recognize and respond to suspicious activity more quickly. To enhance our knowledge, we have recruited industry experts

[2] In accordance with past practice, the SEC's FY 2014 Congressional Budget Justification was submitted by the Chair and was not voted on by the full Commission. The budget request can be found at http://sec.gov/about/reports/secfy14congbudgjust.shtml.

– non-lawyers with specialized experience in sophisticated products, transactions, and industry practices – to assist us in our investigations.

Enforcement's recent actions reflect an aggressive and continued pursuit of institutions and individuals whose actions contributed to the financial crisis, a focus on exchanges and market structure issues aimed at ensuring a fair securities marketplace, pursuit of investment advisers for fraudulent conduct, and continued efforts to combat insider trading by those who abuse positions of trust and confidence for personal gain. In particular, I would like to highlight the following efforts:

Financial Crisis Cases

The SEC continues to hold accountable individuals and institutions whose misconduct contributed to the financial crisis. The SEC filed an additional 42 financial crisis-related enforcement actions since the beginning of FY 2012. Over the last two-and-a-half years, the SEC has filed 94 such actions against 157 individuals and entities, including 66 CEOs, CFOs, and other senior corporate executives. These crisis-related enforcement actions have resulted in 36 individuals being barred from serving in the securities industry or as officers or directors of public companies, as well as orders of nearly $2.7 billion in financial relief for harmed investors.

Market Structure/Exchanges/Broker-Dealers

To ensure fair trading and equal access to information in the securities markets, the SEC brought significant actions in the past year against stock exchanges, alternative trading platforms, broker-dealers, and other market participants. Noteworthy cases included actions charging:

- the New York Stock Exchange with providing certain customers with favored access to data that could be used to make investment decisions;[3]
- dark pool operator eBX LLC with failing to protect the confidential trading information of its customers;[4]
- brokerage firm Hold Brothers On-Line Investment Services with allowing foreign traders to access the markets and conduct manipulative trading through an illegal practice known as "layering;"[5] and
- Pipeline Trading Systems LLC and two of its top executives with failing to disclose to its customers that most orders placed on the dark pool trading platform were filled by a trading operation affiliated with Pipeline.[6]

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[3] Release No. 34-67857, *In the Matter of New York Stock Exchange LLC, et al.* (September 14, 2012), http://www.sec.gov/litigation/admin/2012/34-67857.pdf.

[4] Release No. 34-67969, *In the Matter of eBX, LLC* (October 3, 2012), http://www.sec.gov/litigation/admin/2012/34-67969.pdf.

[5] Release No. 34-67924, *In the Matter of Hold Brothers On-Line Investment Services, LLC, et al.* (September 25, 2012), http://www.sec.gov/litigation/admin/2012/34-67924.pdf.

[6] Release No. 34-65609, *In the Matter of Pipeline Trading Systems LLC, et al.* (October 24, 2011), http://www.sec.gov/litigation/admin/2011/33-9271.pdf.

Insider Trading

The SEC continued its aggressive pursuit of individuals who unlawfully traded on material, non-public information. Many of these actions have involved financial professionals, hedge fund managers, corporate insiders and board members, attorneys or other service professionals who unlawfully tipped or traded on material, non-public information.

Recent examples of insider trading actions include an action against a former senior audit partner at KPMG for tipping his friend with confidential details about five of KPMG's audit clients;[7] a portfolio manager at hedge fund advisory firm Sigma Capital Management who traded on inside information ahead of quarterly earnings announcements by two prominent publicly-traded technology companies;[8] and a former portfolio manager of CR Intrinsic Investors LLC in a $276 million insider trading scheme involving a clinical trial for an Alzheimer's drug.[9]

Investment Advisers

In FY 2012, the SEC filed 147 actions against investment advisers, the most ever in a single year. Several of these actions resulted from risk-based investigations, which are proactive measures to identify misconduct at an early stage so that timely action can be taken and investor losses minimized. The SEC also filed multiple actions arising from an initiative to identify investment advisers who lacked effective compliance programs[10] as well as an investigative initiative into abnormal performance returns by hedge funds.[11]

Cross Border Working Group

Another risk-based initiative that resulted in significant recent actions is the Cross Border Working Group,[12] which focuses on U.S. companies with substantial foreign operations, particularly in China. Through the Cross Border Working Group, the SEC has filed fraud cases involving more than 40 issuers and executives, and deregistered the securities of more than 50 companies. In February, the SEC charged Keyuan Petrochemicals, a China-based company, and

[7] Litigation Release No. 22670, *SEC v. Scott London, et al.* (April 11, 2013), http://www.sec.gov/litigation/litreleases/2013/lr22670.htm.

[8] *SEC v. Michael Steinberg* (March 29, 2013), http://www.sec.gov/litigation/complaints/2013/comp-pr2013-49.pdf.

[9] Litigation Release No. 22539, *SEC v. CR Intrinsic Investors, LLC, et al.* (November 20, 2012), http://www.sec.gov/litigation/litreleases/2012/lr22539.htm.

[10] Release No. IA-3324, *In the Matter of Asset Advisors, LLC* (November 28, 2011), http://www.sec.gov/litigation/admin/2011/ia-3324.pdf; Release No. 34-65838, *In the Matter of Feltl & Company, Inc.* (November 28, 2011), http://www.sec.gov/litigation/admin/2011/34-65838.pdf; Release No. 34-65837, *In the Matter of OMNI Investment Advisors Inc., et al.* (November 28, 2011), http://www.sec.gov/litigation/admin/2011/34-65837.pdf.

[11] Litigation Release No. 22176, *SEC v. Michael R. Balboa, et al.* (December 2, 2011), http://www.sec.gov/litigation/litreleases/2011/lr22176.htm; Litigation Release No. 22151, *SEC v. Chetan Kapur, et al.* (November 10, 2011), http://www.sec.gov/litigation/litreleases/2011/lr22151.htm; Litigation Release No. 22167, *SEC v. Patrick G. Rooney, et al.*(November 22, 2011), http://www.sec.gov/litigation/litreleases/2011/lr22167.htm; Release No. 34-65750, *In the Matter of LeadDog Capital Markets, LLC, et al.* (November 15, 2011), http://www.sec.gov/litigation/admin/2011/33-9277.pdf.

[12] The Cross Border Working Group is an intra-agency group with representatives from each of the SEC's major divisions and offices.

its former CFO with accounting and disclosure violations, resulting in penalties of more than $1 million.[13]

FCPA Manual

In November 2012, the staff of the SEC and the Department of Justice issued a 120-page guide providing detailed analysis of the U.S. Foreign Corrupt Practices Act.[14] The guide details the SEC and DOJ approach to FCPA enforcement and addresses a wide variety of topics relevant to compliance with the law. The guide, which is available on the SEC's website at http://www.sec.gov/spotlight/fcpa/fcpa-resource-guide.pdf, is a helpful resource to companies doing business overseas and should further our goals of education and deterrence.

Guidance on the Use of Social Media by Public Companies

In early April, the SEC provided guidance to public companies about the use of social media for company announcements. In a report issued pursuant to Section 21(a) of the Securities Exchange Act of 1934, the SEC made clear that companies can use social media, such as Facebook and Twitter, to announce key information in compliance with the federal securities laws so long as investors have been alerted about which social media outlets will be used to disseminate such information.[15] The report clarified that issuer communications through social media channels require careful Regulation FD analysis comparable to communications through more traditional channels, and that the principles outlined in the Commission's earlier guidance on Regulation FD apply with equal force to corporate disclosures made through social media channels.[16]

Cooperation

The SEC's Cooperation Program provides incentives to individuals and companies who come forward and provide valuable information in our investigations. The program gives us access to high-quality evidence, resulting in stronger cases that shut down fraudulent schemes earlier than would otherwise be possible. Last month, the Commission announced a non-prosecution agreement with Ralph Lauren Corporation in which the SEC decided not to charge the company with FCPA violations because of its extensive, thorough, and real-time self-reporting and cooperation with the SEC's investigation, thereby demonstrating the substantial and tangible benefits of cooperation.[17]

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[13] Litigation Release No. 22627, *SEC v. Keyuan Petrochemicals, Inc., et al.* (February 28, 2013), http://www.sec.gov/litigation/litreleases/2013/lr22627.htm.

[14] *SEC and Justice Department Release FCPA Guide (November 14, 2012)*, http://www.sec.gov/news/press/2012/2012-225.htm.

[15] Release No. 34-69279, *Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934: Netflix, Inc., and Reed Hastings* (April 2, 2013), http://www.sec.gov/litigation/investreport/34-69279.htm.

[16] *Id.*, at 5.

[17] *SEC Announces Non-Prosecution Agreement with Ralph Lauren Corporation Involving FCPA Misconduct* (April 22, 2013), http://www.sec.gov/news/press/2013/2013-65.htm.

Office of the Whistleblower

The SEC's whistleblower program established pursuant to the Dodd-Frank Act has resulted in investigative staff receiving a substantial volume of high quality information about potential securities laws violations. It has allowed our investigative staff to work more efficiently and permitted us to better utilize agency resources. As set forth in the SEC's Office of the Whistleblower Annual Report for 2012,[18] the Commission received 3,001 tips from whistleblowers in the U.S. and 49 other countries. In August 2012, the Commission made its first award under the whistleblower program.[19]

Inspection and Examination Program

The Office of Compliance Inspections and Examinations (OCIE) is responsible for the Commission's examination and inspection program. OCIE examines securities firms registered with the Commission, including broker-dealers, municipal securities dealers, self-regulatory organizations (SROs), clearing agencies, transfer agents, investment advisers, and investment companies. Additionally, the Dodd-Frank Act increased OCIE's responsibilities to include examinations of, among others, municipal advisors, investment advisers to certain private funds, security-based swap dealers, security-based swap data repositories, major security-based swap participants, and securities-based swap execution facilities. The examination program plays a critical role in supporting compliance within the securities industry, which in turn also helps to protect investors and the securities markets generally.

OCIE has adopted a risk-based examination approach to select firms for examination, the areas of the firm examined, and the issues covered. These examinations are conducted across the country through the Commission's National Examination Program (NEP). In FY 2012, examiners conducted approximately 1,600 examinations, including 443 broker-dealer, 974 investment adviser, 104 investment company complex, 42 transfer agent, and five clearing agency examinations. The staff also conducted 38 market oversight program inspections. Some of the NEP's recent key efforts include the following:

Presence Examinations of Newly Registered Investment Advisers

Initiated in FY 2012 (and more fully integrated in FY 2013), the NEP launched a coordinated national examination initiative designed to establish a meaningful presence with newly registered advisers (the "presence exam initiative").[20] Since the effective date of the Dodd-Frank Act, approximately 1,500 advisers to hedge funds and private equity funds have registered with the SEC for the first time. The presence exam initiative hopes to reach a significant percentage (at least 15 to 25 percent) of these advisers by the end of FY 2014 and is intended, among other things, to assess their commitment to compliance and to meeting their

[18] The 2012 report is available at http://www.sec.gov/about/offices/owb/annual-report-2012.pdf.

[19] Release No. 34-67698, *In the Matter of the Claim for Award in connection with [Non-Public]* (August 21, 2012), http://www.sec.gov/rules/other/2012/34-67698.pdf.

[20] The letter sent to registrants describing the presence exam initiative is available at http://www.sec.gov/about/offices/ocie/letter-presence-exams.pdf.

obligations under the federal securities laws; raise firms' awareness about certain higher-risk areas identified; and generate a proactive effort in firms' compliance departments to strengthen controls and policies on issues beyond the scope of these limited-focus examinations.

Beyond this, the NEP seeks to prioritize examinations where the staff's analytics indicate higher risks to investors relative to the rest of the registrant population, or find indicia of fraud or other serious wrongdoing. OCIE recently issued a risk alert on compliance with the SEC's custody rule for investment advisers.[21] The alert came after a review of recent examinations that identified significant custody-related issues in about one-third of the firms examined.

Developing Examination Staff Expertise

Following the establishment in the NEP in FY 2011 of specialized working groups in key areas including derivatives, hedge funds, private equity, valuation, new and structured products, market structure and trading practices, fixed income and municipal securities, risk management, quantitative analytics and technology, OCIE has continued recruitment of industry experts who bring deep technical experience to our exam program in these areas. A new Quantitative Analytics Unit (QAU) also gives the NEP the expertise to engage and examine the most sophisticated investment firms and programs, including the expertise to identify and understand risks in the algorithms, models, and software on which our registrants increasingly rely for investment decision-making and trading. Additionally, the NEP continued developing a Certified Examiner Training program that will enhance examiner skills, expertise and provide ongoing technical and leadership training.

Other Initiatives

Beyond this, the NEP, among other things:

- recently issued the first public annual statement of examination program goals, setting forth examination priorities and focus areas for the exam program;[22]
- recently implemented a new internal compliance and ethics program to monitor performance and ensure quality and accountability;
- continued to streamline and automate the exam process through the updating of a web-based exam documentation and workpaper retention program; and
- continued to improve coordination with other regulators, including other federal and state regulators as well as counterparts in other countries.

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[21] *Significant Deficiencies Involving Adviser Custody and Safety of Client Assets* (March 4, 2013), http://www.sec.gov/about/offices/ocie/custody-risk-alert.pdf.

[22] *Examination Priorities for 2013* (February 21, 2013), http://www.sec.gov/about/offices/ocie/national-examination-program-priorities-2013.pdf.

Issuer Disclosure and Capital Formation

The Division of Corporation Finance (Corporation Finance) regularly and systematically reviews the disclosures and financial statements of reporting companies as required by the Sarbanes-Oxley Act of 2002, and selectively reviews documents that companies file when they engage in public offerings, business combination transactions, and proxy solicitations to ensure that investors have access to material information for informed investment and voting decisions. Corporation Finance also maintains specialized offices with legal and accounting experts that support filing reviews, undertake reviews of specialized filings, provide interpretive guidance on rules and regulations, participate in Commission rulemaking projects, and provide specialized expertise in enforcement matters. Below is an overview of several key Corporation Finance initiatives.

Dodd-Frank Act Rulemakings

Since its passage, the Commission has adopted Dodd-Frank Act rules regarding accredited investors,[23] say-on-pay,[24] asset-backed securities,[25] compensation committee listing standards and disclosure,[26] conflict minerals,[27] and payments by resource extraction issuers.[28] Corporation Finance and other Commission staff and the Commission continue to work to implement provisions of the Dodd-Frank Act relating to asset-backed securities,[29]

[23] *See* Section 413(a) of the Dodd-Frank Act and Release No. 33-9287, *Net Worth Standard for Accredited Investors* (December 21, 2011), http://www.sec.gov/rules/final/2011/33-9287.pdf.

[24] *See* Section 951 of the Dodd-Frank Act and Release No. 33-9178, *Shareholder Approval of Executive Compensation and Golden Parachute Compensation* (January 25, 2011), http://www.sec.gov/rules/final/2011/33-9178.pdf.

[25] *See* Section 942(a) of the Dodd-Frank Act and Release No. 34-65148, *Suspension of the Duty to File Reports for Classes of Asset-Backed Securities under Section 15(d) of the Securities Exchange Act of 1934* (August 17, 2011), http://www.sec.gov/rules/final/2011/34-65148.pdf; Section 943 of the Dodd-Frank Act and Release No. 33-9175, *Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act* (January 20, 2011), http://www.sec.gov/rules/final/2011/33-9175.pdf; Section 945 of the Dodd-Frank Act and Release No. 33-9176, *Issuer Review of Assets in Offerings of Asset-Backed Securities* (January 20, 2011), http://www.sec.gov/rules/final/2011/33-9176.pdf.

[26] *See* Section 952 of the Dodd-Frank Act and Release No. 33-9330, *Listing Standards for Compensation Committees* (June 20, 2012), http://www.sec.gov/rules/final/2012/33-9330.pdf.

[27] *See* Section 1502 of the Dodd-Frank Act and Release No. 34-67716, *Conflict Minerals* (August 22, 2012), http://www.sec.gov/rules/final/2012/34-67716.pdf.

[28] *See* Section 1504 of the Dodd-Frank Act and Release No. 34-67717, *Disclosure of Payments by Resource Extraction Issuers* (August 22, 2012), http://www.sec.gov/rules/final/2012/34-67717.pdf.

[29] *See* Release No. 34-64148, *Credit Risk Retention* (March 30, 2011), http://www.sec.gov/rules/proposed/2011/34-64148.pdf and Release No. 34-65355, *Prohibition against Conflicts of Interest in Certain Securitizations* (September 19, 2011), http://www.sec.gov/rules/proposed/2011/34-65355.pdf.

disqualifications for felons and other bad actors,[30] executive compensation matters,[31] and credit risk retention in asset-backed securities.[32]

JOBS Act Rulemakings

Corporation Finance is responsible for several Commission mandates under the JOBS Act. Rulewriting teams have been working on recommendations for the Commission's consideration with respect to JOBS Act rulemakings concerning general solicitation, crowdfunding, a new small offering exemption for up to $50 million, and thresholds for registration and deregistration under Section 12(g) of the Exchange Act.[33]

In August 2012, pursuant to Title II of the JOBS Act, the Commission proposed rules to allow general solicitation and general advertising for offers and sales made under Rule 506, provided that all securities purchasers are accredited investors and issuers take reasonable steps to verify that purchasers are accredited investors.[34] The comment period for the proposal ended in October 2012. The Commission and Corporation Finance staff continue to work on implementing this provision of the JOBS Act.

In addition to requiring the Commission to conduct rulemakings, the JOBS Act required the Commission to conduct several studies. The Commission was required to examine its authority to enforce the anti-evasion provisions of Exchange Act Rule 12g5-1 and submit recommendations to Congress.[35] A report on the study was submitted to Congress in October 2012.[36] Corporation Finance also assisted in conducting a study on the transition to trading and quoting securities in one penny increments – also known as decimalization – and the impact decimalization has had on the number of initial public offerings since its implementation.[37] The report was submitted to Congress in July 2012.[38] Finally, the JOBS Act required a review of Regulation S-K to determine how it may be modernized and simplified to reduce the costs and

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[30] *See* Section 926 of the Dodd-Frank Act and Release No. 33-9211, *Disqualification of Felons and Other "Bad Actors" from Rule 506 Offerings* (May 25, 2011), http://www.sec.gov/rules/proposed/2011/33-9211.pdf.

[31] *See* Sections 953(a), 953(b), 954 and 955 of the Dodd-Frank Act.

[32] *See* Section 941 of the Dodd-Frank Act. This was a joint rulemaking with other federal agencies.

[33] *See* Titles II, III, IV, V and VI of the JOBS Act, respectively.

[34] *See* Section 201(a) of the JOBS Act and Release No. 33-9354, *Eliminating the Prohibition against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings* (August 29, 2012), http://www.sec.gov/rules/proposed/2012/33-9354.pdf.

[35] *See* Section 504 of the JOBS Act.

[36] *See Report on Authority to Enforce Exchange Act Rule 12g5-1 and Subsection (b)(3)* (October 15, 2012), http://www.sec.gov/news/studies/2012/authority-to-enforce-rule-12g5-1.pdf. The staff concluded that the current enforcement tools available to the Commission are adequate to enforce the anti-evasion provision of Rule 12g5-1 and determined not to make any legislative recommendations regarding enforcement tools relating to Rule 12g5-1(b)(3).

[37] *See* Section 106(b) of the JOBS Act.

[38] *See Report to Congress on Decimalization* (July 2012), http://www.sec.gov/news/studies/2012/decimalization-072012.pdf.

other burdens for emerging growth companies.[39] The staff is in the process of preparing its recommendations and is working to complete its review in the near future.

Trading and Markets Oversight and Rulemaking

The Division of Trading and Markets (Trading and Markets) seeks to establish and maintain standards for fair, orderly, and efficient markets, while fostering investor protection and confidence in the markets. Trading and Markets supervises the major participants in the U.S. securities markets, and also works closely with the Commission's Office of Credit Ratings to supervise 10 nationally recognized statistical rating organizations (NRSROs) and with the Office of Municipal Securities to supervise the Municipal Securities Rulemaking Board (MSRB) and municipal advisors.

The Dodd-Frank Act and the JOBS Act added substantial new responsibilities to Trading and Market's portfolio, with the division being responsible for more than 30 separate rulemaking initiatives and studies under the two statutes, including a number that will create new ongoing supervisory responsibilities upon completion. I would like to highlight several of these activities.

Market Structure

Addressing Extraordinary Market Volatility. In the wake of the May 6, 2010 "Flash Crash," Trading and Markets took the lead on several Commission actions to address extraordinary market volatility. Most recently, these actions included approval of a National Market System (NMS) Plan to implement a "limit up-limit down" mechanism to create "speed bumps" to limit abrupt market movements in individual securities,[40] and amendments to the market-wide circuit breakers to provide for brief, coordinated, cross-market trading halts during a sharp decline in the

[39] *See* Section 108 of the JOBS Act.

[40] *See* Release No. 67091, *Order Approving, on a Pilot Basis, the National Market System Plan to Address Extraordinary Market Volatility by BATS Exchange, Inc., BATS Y-Exchange, Inc., Chicago Board Options Exchange, Incorporated, Chicago Stock Exchange, Inc., EDGA Exchange, Inc., EDGX Exchange, Inc., Financial Industry Regulatory Authority, Inc., NASDAQ OMX BX, Inc., NASDAQ OMX PHLX LLC, The Nasdaq Stock Market LLC, National Stock Exchange, Inc., New York Stock Exchange LLC, NYSE MKT LLC, and NYSE Arca, Inc.* (May 31, 2012), http://www.sec.gov/rules/sro/nms/2012/34-67091.pdf; Release No. 34-68953, *Notice of Filing and Immediate Effectiveness of the Second Amendment to the Limit Up-Limit Down Plan* (February 20, 2013), http://www.sec.gov/rules/sro/nms/2013/34-68953.pdf; Release No. 34-69287, *Order Approving the Third Amendment to the Limit Up-Limit Down Plan* (April 3, 2013), http://www.sec.gov/rules/sro/nms/2013/34-69287.pdf.

securities market.[41] The market-wide circuit breakers and phase I of the NMS Plan relating to the limit up-limit down mechanism were implemented on April 8, 2013.[42]

Enhancing Access to Market Data. Trading and Markets also has facilitated a number of important initiatives to significantly improve the Commission's access to market data, including:

- rules to require SROs to submit a plan to create, implement, and maintain a consolidated audit trail (CAT) that would allow regulators to track all activity throughout the U.S. markets in exchange-traded equity securities (approved July 2012);[43]

- rules to capture additional information on certain large traders (approved July 2011), with phase I of the reporting and recordkeeping requirements becoming effective on November 30, 2012;[44]

- establishing a new Office of Analytics and Research (OAR), which is responsible for developing new market data sources and analyses to aid the Commission's supervision of the securities markets; and

- implementation by OAR of a new Market Information Data Analytics System (MIDAS) to collect and analyze market data from both the public consolidated data feeds and the "proprietary" data feeds offered by the exchanges to their customers.

Preserving Technological Integrity. In addition to reducing effects of individual disruptions, the Commission is committed to attacking the causes and reducing the number of disruptions by fostering a robust infrastructure through a focus on systems compliance and integrity. Among other steps taken to strengthen technology standards among exchanges and other key participants, in March 2013 the Commission proposed Regulation SCI, which, among other things, would require that exchanges and other key market players maintain policies and

[41] *See* Release No. 34–67090, *Notice of Filing of Amendments No. 1 and Order Granting Accelerated Approval of Proposed Rule Changes as Modified by Amendments No. 1, Relating to Trading Halts Due to Extraordinary Market Volatility* (May 31, 2012), http://www.sec.gov/rules/sro/bats/2012/34-67090.pdf. The operative date of the revised circuit breakers was delayed from February 4, 2013 to April 8, 2013. *See, e.g.*, Release No. 34–68784, *Notice of Filing and Immediate Effectiveness of Proposed Rule Change Delaying the Operative Date of A Rule Change to NYSE Rule 80B, Which Provides for Methodology for Determining When to Halt Trading in All Stocks Due to Extraordinary Market Volatility, From the Date of February 4, 2013, Until April 8, 2013* (January 31, 2013), http://www.sec.gov/rules/sro/nyse/2013/34-68784.pdf.

[42] Phase I applies the limit up-limit-down mechanism to stocks in the S&P 500, the Russell 1000, and to select exchange-traded products. Phase II, currently scheduled for implementation in November 2013, will apply to all remaining exchange-traded equity securities, and will be implemented six months following the implementation of Phase I.

[43] *See* Release No. 34-67457, *Consolidated Audit Trail* (July 18, 2011), http://www.sec.gov/rules/final/2012/34-67457.pdf.

[44] *See* Release No. 34-64976, *Large Trader Reporting* (July 27, 2011), http://www.sec.gov/rules/final/2011/34-64976.pdf.

procedures reasonably designed to meet certain technology standards and that these entities take appropriate corrective action if problems do occur.[45]

OTC Derivatives

Trading and Markets also has continued to engage in rulemaking to establish a new oversight regime for the OTC derivatives marketplace. To date, the Commission has proposed substantially all of the core rules required by Title VII of the Dodd-Frank Act, adopted a number of final rules and interpretations, provided a "roadmap" to implementation of Title VII, and taken other actions to provide legal certainty to market participants during the implementation process. Recent initiatives include:

- proposed rules regarding the application of Title VII in the cross-border context (May 2013);[46]
- proposed core financial responsibility rules for security-based swap dealers and major security-based swap participants (October 2012);[47]
- final rules and interpretations adopted jointly with the CFTC regarding key product definitions under Title VII (July 2012);[48]
- final rules and interpretations adopted jointly with the CFTC regarding entity definitions under Title VII (April 2012);[49]
- final rules adopted to establish operational and risk management standards for clearing agencies, including clearing agencies that clear security-based swaps (October 2012);[50] and

[45] *See* Release No. 34-69077, *Regulation Systems Compliance and Integrity* (March 8, 2013), http://www.sec.gov/rules/proposed/2013/34-69077.pdf.

[46] *See* Release No. 34-69490, *Cross-Border Security-Based Swap Activities; Re-Proposal of Regulation SBSR and Certain Rules and Forms Relating to the Registration of Security-Based Swap Dealers and Major Security-Based Swap Participants* (May 1, 2013), http://www.sec.gov/rules/proposed/2013/34-69490.pdf.

[47] *See* Release No. 34-68071, *Capital, Margin, and Segregation Requirements for Security-Based Swap Dealers and Major Security-Based Swap Participants and Capital Requirements for Broker-Dealers* (October 18, 2012), http://www.sec.gov/rules/proposed/2012/34-68071.pdf.

[48] *See* Release No. 33-9338, *Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping* (July 18, 2012), http://www.sec.gov/rules/final/2012/33-9338.pdf.

[49] *See* Release No. 34-66868, *Further Definition of "Swap Dealer," "Security-Based Swap Dealer," "Major Swap Participant," "Major Security-Based Swap Participant" and "Eligible Contract Participant* (April 27, 2012), http://www.sec.gov/rules/final/2012/34-66868.pdf.

[50] *See* Release No. 34-68080, *Clearing Agency Standards* (October 22, 2012), http://www.sec.gov/rules/final/2012/34-68080.pdf.

- final rules adopted to establish procedures for the Commission's review of certain actions undertaken by clearing agencies (June 2012).[51]

Trading and Markets expects in the near term to make recommendations to the Commission regarding a rule proposal relating to books and records and reporting requirements for security-based swap dealers and major security-based swap participants. It also is likely that the Commission will consider the application of mandatory clearing requirements to single-name credit default swaps, starting with those that were first cleared prior to the enactment of the Dodd-Frank Act.[52]

Trading and Markets staff is also continuing to develop recommendations for final rules required by Title VII that have been proposed but not yet adopted.

The Volcker Rule

Section 619 of the Dodd-Frank Act generally prohibits banks and their affiliates from engaging in proprietary trading, and also prohibits these entities from sponsoring or investing in a hedge fund or private equity fund. Also known as the Volcker Rule, the statute provides limited exceptions to the prohibition on proprietary trading for: (1) underwriting; (2) market making-related activities; (3) risk-mitigating hedging; (4) trading in certain government obligations; and (5) trading on behalf of customers.

In October 2011, the federal banking agencies and SEC jointly proposed rules to implement the Volcker Rule.[53] In January 2012, the CFTC issued a substantially similar proposal. To date, we have received over 19,000 comment letters in response to the proposal. Going forward, SEC staff will continue to engage in regular and active consultation with the staffs at our fellow federal financial regulators in order to develop recommendations for implementing Section 619 of the Dodd-Frank Act.

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[51] *See* Release No. 34-67286, *Process for Submissions for Review of Security-Based Swaps for Mandatory Clearing and Notice Filing Requirements for Clearing Agencies; Technical Amendments to Rule 19b-4 and Form 19b-4 Applicable to All Self-Regulatory Organizations* (June 28, 2012), http://www.sec.gov/rules/final/2012/34-67286.pdf.

[52] Clearing of credit default swaps commenced in 2009. The Commission issued a series of temporary conditional exemptions to help provide legal certainty to facilitate those clearing activities, in light of issues regarding the potential that cleared credit default swaps would be "securities" subject to the Commission's authority under the Exchange Act. See, e.g., Release No. 34-63387, *Order Extending and Modifying Temporary Exemptions Under the Securities Exchange Act of 1934 in Connection with Request of ICE Trust U.S. LLC Related to Central Clearing of Credit Default Swaps and Request for Comment* (November 29, 2010) (temporary exemption in connection with clearing by ICE Trust, now ICE Clear Credit), http://www.sec.gov/rules/exorders/2010/34-63387.pdf; Release No. 34-63389, *Order Extending Temporary Conditional Exemptions Under the Securities Exchange Act of 1934 in Connection with Request on Behalf of ICE Clear Europe, Limited Related to Central Clearing of Credit Default Swaps and Request for Comment* (November 29, 2010) (temporary exemption in connection with clearing by ICE Clear Europe), http://www.sec.gov/rules/exorders/2010/34-63389.pdf.

[53] *See* Release No. 34-65545, *Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships With, Hedge Funds and Private Equity Funds* (October 12, 2011), http://www.sec.gov/rules/proposed/2011/34-65545.pdf.

Future Initiatives. Trading and Markets staff expects to engage in the following initiatives, among others, to address developments and issues in the exchange and OTC markets for securities:

- publishing reports concerning liquidity, volatility, and other market characteristics both to expand the amount of publicly available information on these topics and to establish a more sound empirical basis for future market structure initiatives;
- considering what, if any, actions to take concerning trading, liquidity, transparency, and other market characteristics under the current market structure;
- monitoring the SROs in their implementation of the CAT;
- monitoring the impact of the limit up-limit down mechanism and market-wide circuit breakers, including working with the SROs to determine whether additional measures may be necessary to address extraordinary market volatility;
- evaluating how to improve the market structure for trading fixed income securities generally, including the trading of municipal and corporate bonds;
- reevaluating Trading and Market's approach in reviewing new exchange-traded products;
- continuing to monitor broker-dealers that use value-at-risk models to calculate net capital, which includes the largest and most systemically important firms, and expanding risk oversight to include security-based swap dealers; and
- expanding the Commission's oversight of existing clearing agencies, particularly those that are designated as systemically important by the Financial Stability Oversight Council (FSOC).

Investment Management Oversight and Rulemaking

The SEC's Division of Investment Management (Investment Management) works to protect investors, promote informed investment decisions, and facilitate appropriate innovation in investment products and services through oversight and regulation of the asset management industry. Investment Management primarily administers the SEC's regulatory and disclosure-review functions for mutual funds, other investment companies, and investment advisers, including registration requirements. As part of these functions, the Commission and the Division oversee funds with a combined $15 trillion in assets under management and registered investment advisers with over $50 trillion in assets under management. The Commission already implemented the vast majority of the Dodd-Frank Act's mandates related to funds and advisers, including rules to effectuate private fund adviser registration and reporting,[54] implementing new

[54] Release No. IA-3221, *Rules Implementing Amendments to the Investment Advisers Act of 1940* (June 22, 2011), http://www.sec.gov/rules/final/2011/ia-3221.pdf.

registration exemptions for certain advisers,[55] reallocating responsibility for smaller advisers to the state securities authorities,[56] and amending requirements for advisers that charge performance fees.[57]

Private Fund Adviser Regulation

The staff has been actively engaged with advisers to hedge funds and other private funds as they register with the SEC pursuant to the rules the Commission adopted to implement the Dodd-Frank Act's adviser registration mandate. The SEC now has an adviser population that includes approximately 40 percent of SEC-registered advisers managing at least one private fund, which presents several challenges, including the fact that these advisers generally are more complex and require greater resources to examine. Additionally, the staff is examining many of the SEC's existing rules applicable to advisers that were not written with private fund advisers necessarily in mind.

Throughout the past year, SEC staff has been assisting private fund advisers as they file their initial Form PF data. Form PF is a confidential data reporting form providing data about private funds' risk characteristics.[58] The form was developed by the SEC and the CFTC, in consultation with FSOC, pursuant to a Dodd-Frank Act mandate. We are starting to use the data collected on Form PF to assist us in carrying out our regulatory mission, and going forward, we will seek to expand and improve our use of it, while also sharing the information with FSOC for their systemic risk analysis functions as contemplated by the Dodd-Frank Act.

Money Market Funds

A rule proposal pertaining to money market mutual fund reform is well underway at the SEC and has been the product of a comprehensive and collaborative process. Any proposal that results would seek to preserve many of the benefits of money market funds for investors and the short-term funding markets while lessening money market funds' susceptibility to runs; improving their ability to manage and mitigate potential contagion from high levels of redemptions; and increasing the transparency of their risks.

Identity Theft Red Flags

On April 10, 2013, my first day as Chair, the Commission unanimously voted to adopt a joint rule with the CFTC that fulfilled the Dodd-Frank Act mandate to transfer regulatory and enforcement authority for identity theft red flag programs from the Federal Trade Commission to

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[55] Release No. IA-3222, *Exemptions for Advisers to Venture Capital Funds, Private Fund Advisers with Less Than $150 Million in Assets under Management, and Foreign Private Advisers* (June 22, 2011), http://www.sec.gov/rules/final/2011/ia-3222.pdf.

[56] Release No. IA-3221, *Rules Implementing Amendments to the Investment Advisers Act of 1940* (June 22, 2011), http://www.sec.gov/rules/final/2011/ia-3221.pdf.

[57] Release No. IA-3372, *Investment Adviser Performance Compensation* (February 15, 2012), http://www.sec.gov/rules/final/2012/ia-3372.pdf.

[58] Release No. IA-3308, *Reporting by Investment Advisers to Private Funds and Certain Commodity Pool Operators and Commodity Trading Advisors on Form PF* (October 31, 2011), http://www.sec.gov/rules/final/2011/ia-3308.pdf.

the SEC and CFTC for the entities each agency regulates.[59] The rule will help protect investors from identity theft by requiring that broker-dealers, mutual funds, and certain other SEC-regulated entities create programs to detect and respond appropriately to red flags.

Updated Valuation Guidance

Investment Management also is seeking to update and put in one place guidance available to funds and their boards of directors as they value portfolio holdings and calculate a daily net asset value – the price at which most mutual funds transact. The bulk of the existing Commission guidance in this area was issued in 1970, long before the advent of significant derivatives investing, the emergence of pricing services, or the development of complex pricing techniques.[60] Investment Management and other SEC staff have been meeting with interested parties to develop a recommendation of updated fund valuation guidance for the Commission's consideration.

Risk and Exam Office

Investment Management recently established a new Risk and Exam Office (REO) dedicated to risk analysis and examination of funds and investment advisers. Examiners are included within REO to give effect to the Dodd-Frank Act's mandate that examiners be included within the Division of Investment Management. It is expected that the work of the REO's new examiners will inform the division's regulatory initiatives. In addition, REO's mission is to conduct rigorous quantitative and qualitative financial analysis of the investment management industry. This should greatly improve the staff's analytical capability with respect to asset managers.

Risk Data and Economic Analysis

The Division of Risk, Strategy, and Financial Innovation (RSFI) was formed in September 2009 in part to integrate rigorous data analytics into the core mission of the SEC. RSFI has a broad role in Commission activities, interacting with nearly every Division and Office. Much of RSFI's staff time is dedicated to developing economic analysis in connection with Commission rulemaking. In addition, the Division provides economic research, risk assessment, and data analysis to help focus the agency's resources on matters presenting the greatest perceived risks in litigation, examinations, and registrant reviews.

As the Commission undertakes additional rulemaking and evaluates existing rules, continued access to robust, data-driven economic analyses is necessary to develop efficient rules and evaluate the effectiveness of our existing regulations. Over the past year, the SEC has refocused its efforts on ensuring that rigorous and transparent economic analysis is incorporated

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[59] Release No. IA-3582, *Identity Theft Red Flag Rules* (April 10, 2013), http://sec.gov/rules/final/2013/34-69359.pdf.

[60] Release No. IC-6295, *Accounting for Investment Securities by Registered Investment Companies* (Dec. 23, 1970), http://www.sec.gov/rules/interp/1970/ic-6295.pdf; Release No. IC-5847, *Statement Regarding "Restricted Securities"* (Oct. 21, 1969), http://www.sec.gov/rules/interp/1969/ic-5847.pdf.

throughout the rulewriting process. For example, last year RSFI analyzed voluminous data to examine the amount of CDS dealing activity that would be covered by a Dodd-Frank Act-mandated rule further defining "security-based swap dealer" and "major security-based swap participant," and the amount of dealing activity that would be unregulated under various de minimis thresholds.[61] This analysis was the foundation for the Commission's decision to provide a de minimis threshold of the size included in the final rule.[62]

RSFI economists also have made important contributions to pre-proposal rule development. For example, RSFI economists performed qualitative and quantitative analyses to study money market funds in order to respond to a series of questions posed by Commissioners. This analysis has assisted the Commission in its deliberations as it considers the scope of any future rulemaking relating to money market funds.[63]

In addition, as the industries we regulate use increasingly sophisticated technology and high-frequency trading algorithms, our ability to use statistical and trend analyses to identify potentially inappropriate or risky industry practices is essential to help inform our enforcement, examination, and rulemaking efforts. RSFI has already shown great success with the development of an analytical model that uses performance data to identify hedge fund advisers worthy of further review by Enforcement or OCIE. Currently, RSFI is developing a new data analytics model that could be used across the SEC to assess the degree to which registrants' financial statements appear anomalous. This "Accounting Quality Model" is intended to be useful to many offices and divisions within the SEC, such as in helping the Division of Enforcement target their investigations and informing the filings review process by the Division of Corporation Finance. Going forward, RSFI plans to continue to develop and implement robust analytical models to identify regulated entities with high-risk profiles.

New Commission Offices

In addition to Enforcement's Office of the Whistleblower discussed above, the Dodd-Frank Act required the Commission to create four new offices: the Office of Credit Ratings, Office of the Investor Advocate, Office of Minority and Women Inclusion, and Office of Municipal Securities.

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[61] RSFI's memorandum, laying out its analysis, was then included in the comment file to ensure its availability for public comment. *See* Memorandum from the Division of Risk, Strategy, and Financial Innovation, *Information regarding activities and positions of participants in the single-name credit default swap market* (March 15, 2012), http://sec.gov/comments/s7-39-10/s73910-154.pdf.

[62] Release No. 34-66868, *Further Definition of "Swap Dealer," "Security-based Swap Dealer," "Major Swap Participant," "Major Security-Based Swap Participant," and "Eligible Contract Participant"* (April 27, 2012), http://sec.gov/rules/final/2012/34-66868.pdf.

[63] *See* Memorandum from the Division of Risk, Strategy, and Financial Innovation, *Response to Questions Posed by Commissioners Aguilar, Paredes, and Gallagher* (November 30, 2012), http://www.sec.gov/news/studies/2012/money-market-funds-memo-2012.pdf.

Office of Credit Ratings

As required by Section 932 of the Dodd-Frank Act, the Commission established an Office of Credit Ratings (OCR) in June 2012. OCR is charged with administering the rules of the Commission with respect to the practices of NRSROs in determining credit ratings, promoting accuracy in credit ratings issued by NRSROs, and ensuring that (1) credit ratings are not unduly influenced by conflicts of interest and (2) firms provide greater disclosure to investors. In support of this mission, OCR monitors the activities and conducts examinations of NRSROs to assess and promote compliance with statutory and Commission requirements.

Under the Dodd-Frank Act, the Commission is required to undertake a number of rulemakings related to NRSROs. The staff is continuing to work to finalize a series of proposed rules intended to strengthen the integrity of credit ratings by, among other things, improving their transparency. The Dodd-Frank Act also mandated three studies relating to credit rating agencies, two of which were published last year,[64] and one of which is due later in 2013.[65]

Additionally, the Dodd-Frank Act required every federal agency to review its regulations that require use of credit ratings as an assessment of the credit-worthiness of a security and undertake rulemakings to remove these references and replace them with other standards of credit-worthiness that the agency determines are appropriate. Beyond the steps the Commission took in 2011 to fulfill this requirement,[66] in 2012 the Commission issued an Interpretive Release that removes references to credit ratings by NRSROs in two definitions in the Exchange Act.[67]

Office of the Investor Advocate

Section 915 of the Dodd-Frank Act required the SEC to establish an Office of the Investor Advocate to assist retail investors in resolving significant problems they may have with the Commission or with SROs. The Investor Advocate also will identify areas in which investors would benefit from changes in Commission regulations or SRO rules; identify problems that investors have with financial service providers and investment products; and analyze the potential impact on investors of proposed Commission regulations and SRO rules. The Investor Advocate also must hire an Ombudsman, whose activities will be included in the Advocate's reports to Congress. The Commission is in the process of filling the position of Investor Advocate.

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[64] *See Credit Rating Standardization Study* (September 2012), http://www.sec.gov/news/studies/2012/939h_credit_rating_standardization.pdf; *Report to Congress on Assigned Credit Ratings* (December 2012), http://www.sec.gov/news/studies/2012/assigned-credit-ratings-study.pdf. For the latter topic, the Commission will be holding a roundtable scheduled for May 14, 2013.

[65] *See* Dodd-Frank Act § 939C.

[66] *Report on Review of Reliance on Credit Ratings* (July 2011), http://www.sec.gov/news/studies/2011/939astudy.pdf.

[67] *See* Release No. 34-67448, *Commission Guidance Regarding Definitions of Mortgage Related Security and Small Business Related Security* (July 17, 2012), http://www.sec.gov/rules/interp/2012/34-67448.pdf.

Office of Minority and Women Inclusion

The Office of Minority and Women Inclusion (OMWI) is responsible for all matters related to diversity in management, employment, and business activities at the SEC. The OMWI Director is responsible for developing standards for equal employment opportunity and diversity of the workforce and senior management of the SEC, the increased participation of minority-owned and women-owned businesses in the SEC's programs and contracts, and assessing the diversity policies and practices of entities regulated by the SEC.[68] OMWI also is required to submit an annual report to Congress on specific actions taken by the agency and OMWI related to minority and women contracting awards, outreach programs, and employee and contractor hiring challenges.[69]

SEC Diversity Efforts. Under a broad outreach strategy developed by OMWI, the SEC has sponsored and/or attended more than 40 career fairs, conferences, and business matchmaking events to market the SEC to diverse suppliers and jobseekers. OMWI also continued to partner with leading organizations focused on developing employment opportunities for minorities and women at the SEC and in the financial services industry. As a result of these efforts, the SEC saw an increase in the percentages of new hires in FY 2012 over FY 2011 for the following demographic groups: African-American/Black; Asian-American; and American Indian/Alaskan Native. There remains more that can be done with respect to diversity in our hiring, however, particularly for attorneys, accountants, and examiners.

SEC Programs and Contracts. OMWI continues to move forward with respect to policies relating to contracting and regulated entities. OMWI staff is preparing to incorporate good faith contract language in the SEC's contracts that seeks to ensure the fair inclusion of women and minorities in the workforce of the contractor. The language will be incorporated in all SEC contracts for services that exceed a certain threshold amount. The OMWI Director also is required to advise the Commission on the impact of the SEC's policies and regulations on minority-owned and women-owned businesses. Of the total $302.4 million awarded to contractors in FY 2012, $64.1 million (21.2%) was awarded to minority-owned and women-owned businesses.

Practices of Regulated Entities. During FY 2012, the OMWI Director and staff participated in roundtable discussions with regulated entities, representative trade associations, community groups, and other interested parties to obtain information about existing diversity policies and leading practices, and to hear their perspectives and suggestions. In FY 2013, OMWI is working with key agency staff to develop proposed standards to assess the diversity policies and practices of SEC-regulated entities, and to solicit feedback from securities and financial services industry groups on the impact of the proposed standards on the entities regulated by the agency.

[68] *See* Dodd-Frank Act, § 342(b)(2).

[69] *Office of Minority and Women Inclusion Annual Report* (April 24, 2013), http://www.sec.gov/news/studies/2013/omwi-annualreport-2013.pdf.

Office of Municipal Securities

Pursuant to Section 979 of the Dodd-Frank Act, the Commission established a separate Office of Municipal Securities (OMS) to administer the Commission's rules on practices of broker-dealers, advisors, investors, and issuers with respect to municipal securities and to coordinate with the MSRB on rulemaking and enforcement actions. OMS advises the Commission and other SEC offices on policy matters, enforcement, current market issues, and other issues affecting the municipal securities market. OMS also serves as the Commission's liaison to the MSRB, FINRA, the IRS Office of Tax-Exempt Bonds, and various industry groups and regulators on municipal securities issues.

The highest immediate priority project for OMS is to finalize permanent rules for the registration of municipal advisors with the SEC pursuant to Section 975 of the Dodd-Frank Act. This new registration requirement, which became effective on October 1, 2010, applies broadly to persons that provide advice to municipal entities on municipal financial products or the issuance of municipal securities or that solicit municipal entities. In September 2010, the Commission adopted, and subsequently extended, temporary rules for municipal advisor registration.[70] In December 2010, the Commission proposed permanent rules for municipal advisor registration.[71] The SEC received over 1,000 comment letters on the proposal. Many expressed concern that the proposed rules were overbroad, including well-publicized concerns about their potential impact on appointed board members of municipal entities, municipal investments unrelated to municipal securities, and traditional banking products and services. The staff is developing a recommendation for final rules that we anticipate will address these concerns.

OMS's current priorities also include initiatives to assist with the ongoing consideration of disclosure and market structure recommendations in the Commission's Report on the Municipal Securities Market, issued in July 2012.[72] Recently, a Commission roundtable discussed, among other things, potential ways to improve the transparency and efficiency of the municipal securities market.

International Affairs

The Office of International Affairs (OIA) advances international enforcement and regulatory cooperation, promotes high quality regulatory standards worldwide, and formulates technical assistance programs to strengthen investor protection and regulatory infrastructure globally. OIA partners with Enforcement to facilitate the assistance of foreign regulators to obtain evidence for use in Enforcement investigations, as well as to trace, freeze and repatriate proceeds of fraud transferred outside the United States. For example, in the Nexen case filed last

[70] *See* Release No. 34-62824, *Temporary Registration of Municipal Advisors* (September 1, 2010), http://www.sec.gov/rules/interim/2010/34-62824.pdf.

[71] *See* Release No. 34-63576, *Registration of Municipal Advisors* (December 20, 2010), http://sec.gov/rules/proposed/2010/34-63576.pdf.

[72] *See Report on the Municipal Securities Market* (July 31, 2012), http://www.sec.gov/news/studies/2012/munireport073112.pdf.

year, crucial assistance from the Hong Kong Securities and Futures Commission enabled the SEC to pursue traders who reaped more than $13 million in illegal profits by trading in advance of an acquisition.[73] The assistance also allowed the SEC to file insider trading charges and obtain an emergency freeze of assets held by traders in Hong Kong and Singapore. At the time the case was filed by the SEC, it was only four days after the acquisition announcement, and the SEC did not know the identities of most of the traders. Following a request facilitated by OIA, the Hong Kong authorities quickly provided the bank, brokerage, and business records necessary to identify the traders and the details of the trades. To date, we have already obtained more than $17 million in disgorgements and monetary penalties in this case as a direct result of international collaboration.

OIA also assists Commission staff in conducting examinations of foreign-domiciled registrants and addressing cross-border registration issues. OIA further facilitates cooperation between the Commission and its counterparts in the oversight of globally active entities, and negotiates supervisory memoranda of understanding (MOUs) on behalf of the Commission with foreign regulators.

OIA seeks to advance the SEC's interests by participating in a wide array of international organizations, including the International Organization of Securities Commissions and the Financial Stability Board. OIA assists the SEC efforts to deal with cross-border regulatory issues by, among other things, analyzing the potential impact of SEC rules and actions on foreign market participants active in U.S. markets and on the cross-border activities of U.S. issuers and financial service providers, and the possible effect that foreign regulators' actions might have on the SEC, the U.S. market and market participants. OIA also monitors foreign regulatory reform efforts to alert the Commission of potential conflicts and opportunities for cross-border coordination.

Accounting and Auditing Oversight

The federal securities laws authorize the Commission to set accounting standards for public companies, and the Commission has recognized the standards set by the Financial Accounting Standards Board (FASB). The Commission's Office of the Chief Accountant, which serves as the principal advisor to the Commission on accounting and auditing matters, oversees the FASB's standard-setting process. The Commission also plays an important role in connection with International Financial Reporting Standards (IFRS), which foreign private issuers can use in their filings with the Commission, including through interaction with the International Accounting Standards Board (IASB) and the Commission's participation in the IFRS Foundation Monitoring Board.

The FASB and the IASB are working together on several projects to set high-quality converged accounting standards in the areas of revenue recognition, financial instruments, leases, and insurance contracts. During 2013, the FASB and the IASB issued proposals for public comment on financial instruments, expect to issue proposals for public comment on leases and

[73] Litigation Release No. 22428, *SEC v. Well Advantage Ltd. et al.*, (July 30, 2012), http://www.sec.gov/litigation/litreleases/2012/lr22428.htm.

insurance contracts, and expect to issue a final standard on revenue recognition. Commission staff is monitoring progress on the projects and remains committed to assuring that the process operates in a fair and open way and that the results serve the interests of investors.

The Public Company Accounting Oversight Board (PCAOB) oversees the audits of issuers and registered broker-dealers to protect the interests of investors and further the public interest in the preparation of informative, accurate, and independent audit reports. The PCAOB accomplishes its objectives through registration, standard setting, inspection, and discipline. The Commission has oversight over the PCAOB, which includes appointing board members, approving PCAOB rules, reviewing PCAOB disciplinary actions and disputes regarding inspection reports, and approving the PCAOB's budget and accounting support fee. The PCAOB has an active standard-setting agenda, including projects to update numerous standards that address important aspects of the performance of audits and a project to consider changes to the content of the auditor's report on a company's financial statements.

Investor Education

The Office of Investor Education and Advocacy (OIEA) seeks to provide individual investors with the information they need to avoid fraud and make sound decisions concerning investments in the securities markets. OIEA administers three primary programs to promote this mission: assisting individual investors with complaints and inquiries; conducting educational outreach; and providing the Commission and staff with input from the perspective of the individual investor.

During FY 2012, OIEA processed almost 30,000 complaints, questions, and other contacts from investors received, and to date in FY 2013 has published 11 alerts and bulletins. OIEA communicates with investors regarding how to invest wisely and avoid fraud through various media, publishes educational materials, leads educational seminars and investor-oriented events, and partners with federal agencies, state regulators, consumer groups, and self-regulatory organizations. OIEA also produces investor alerts and bulletins in coordination with the other offices and divisions, provides input into rulemaking, administers the Investor Advisory Committee, and conducts investor testing, most recently on the usefulness of disclosures in standard SEC disclosure documents. In August 2012, OIEA issued a Dodd-Frank mandated report entitled *Study Regarding Financial Literacy Among Investors.*[74]

Internal Operations

The Office of the Chief Operating Officer (OCOO) leads and coordinates the activities of the Offices of Financial Management (OFM), Information Technology, Acquisitions, Human Resources (OHR), and Support Operations (OSO).

In FY 2012, OFM continued to focus on strengthening internal controls over financial reporting, with the SEC achieving its best ever result in its FY 2012 Government Accountability Office (GAO) financial controls audit. For the second consecutive year, GAO noted no material

[74] *Study Regarding Financial Literacy Among Investors* (August 2012), http://www.sec.gov/news/studies/2012/917-financial-literacy-study-part1.pdf.

weakness and the number of significant deficiencies identified in the SEC's financial operations was reduced. These results occurred during the complex midyear migration of the SEC's financial system to a Federal Shared Services Provider hosted by the Department of Transportation.

Additional activities during FY 2012 included:

- overseeing the reorganizations of OFM, OHR, and the creation of a new OSO organization, all intended to improve customer support and internal operational controls and effectiveness;

- working closely with the General Services Administration to complete the transfer of excess property and on other leasing-related matters;

- coordinating business process redesign efforts in all OCOO offices in an effort to improve efficiency and effectiveness; and

- automating processes that historically have been manual in nature in areas such as filing fees and disgorgements and penalties.

Leveraging Technology

While the agency has made significant progress over the past few years in modernizing our technology systems, it also is important that the SEC continue leveraging technology to streamline operations and increase the effectiveness of the agency's programs. The SEC's FY 2014 budget request includes additional funds for technology to support a number of key Information Technology (IT) initiatives, including enhancements to the system for receiving tips, complaints, and referrals, improvements to IT security, data analysis tools, improvements in our e-Discovery systems, and infrastructure upgrades aimed at achieving efficiencies in business operations and reducing long-term costs.

In FY 2014, the SEC also plans to continue using the SEC Reserve Fund, established by statute, to fund large, multi-year, mission-critical technology projects. Among other projects, the agency would continue overhauling the Electronic Data Gathering, Analysis and Retrieval (EDGAR) system to create a new, modernized system that will meet Commission requirements for real-time system updates, reduce filer burden, improve data capture, and reduce the long term costs of operating and maintaining the system. In addition, we plan to continue construction and enhancement of the Enterprise Data Warehouse (EDW). The EDW is a critical step in combining currently disparate sources of data from EDGAR filings, exam reports, investigations, external vendors, and many other sources. An organized central data repository should allow enhanced analytical capabilities, predictive modeling, and strengthened governance of data controls and quality standards.

FY 2014 Budget Request

The securities markets we oversee are continuously evolving, and the technology of today is most certainly not the technology of tomorrow. Fast-paced and constantly changing

markets – fueled by financial firms whose annual technology budgets exceed what the SEC spends on its entire operations – require constant monitoring and analysis. When issues are identified, the investing public deserves appropriate and timely regulatory and enforcement responses. The securities industry also has been growing rapidly in size. In the last decade, trading volume in the equity markets has more than doubled, as have assets under management by investment advisers. It is expected that these trends will continue in the foreseeable future. At the same time, the SEC's jurisdiction has grown to cover significant new aspects of the securities markets.

Although the agency has made significant strides forward to strengthen its oversight over markets that are so critical to the savings of American families and to the growth potential of American businesses, much work remains.

The SEC's current level of resources presents significant challenges as we seek to keep pace with the growing size and complexity of the securities markets and fulfill our broad mandates and responsibilities. The FY 2014 budget request – all of which would be fully offset by matching collections of fees on securities transactions and will not increase the Federal budget deficit – seeks to address these challenges directly, to better position the agency to provide the kind of market oversight that the public expects and deserves.

The SEC is requesting $1.674 billion for FY 2014. If enacted, this request would permit us to add approximately 676 new staff positions, which are needed today both to improve core operations and implement the agency's new responsibilities. The budget request would provide additional funding for the following key areas:

- expanding oversight of investment advisers and improving their regulation and compliance;
- bolstering enforcement;
- economic and risk analysis to support rulemaking and oversight;
- building oversight of derivatives and clearing agencies;
- enhancing reviews of corporate disclosures, including supporting implementation of the JOBS Act;
- leveraging technology, including enhancing the tips, complaints, and referrals system, building data analysis tools, improving our e-Discovery systems, and bolstering IT security; and
- enhancing training and development of SEC staff.

Conclusion

Thank you for your support for the agency's mission and for inviting me to be here today to discuss the many initiatives of the SEC. 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 improvements we have made to date.

I am happy to answer any questions you may have.

SPENCER BACHUS
6TH DISTRICT, ALABAMA

COMMITTEES:
FINANCIAL SERVICES
CHAIRMAN EMERITUS

JUDICIARY
SUBCOMMITTEE CHAIRMAN
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March 14, 2013

Chairman Ben Bernanke
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue N.W.
Washington, DC 20551-0001

Chairman Bernanke:

As I mentioned at our recent Humphrey-Hawkins hearing, I am concerned about the Fed's Proposed Rule to implement Section 165 of the Dodd-Frank Act, which would impose enhanced prudential standards and early remediation requirements for foreign banking organizations and foreign nonbank financial companies.

In particular, four things stand out to me. First, the approach taken in the proposed rule towards foreign owned broker-dealers is different from the regulatory regime that would apply to U.S. broker dealers owned by American companies, particularly in the case of a foreign owned broker-dealer not affiliated with a US insured bank. The Fed is taking a distinctly different approach for these foreign-owned firms and US firms will not be forced to have their comparable broker-dealers placed under a new type of intermediate holding company with separate capital, liquidity and other regulatory requirements beyond the SEC's.

Second, the approach would appear highly discriminatory as a foreign owned broker-dealer would have higher capital standards via the intermediate bank holding company and could not rely on its parent's capital to satisfy US requirements, unlike US firms. The long-standing principle of national treatment has been embedded in US law for over 35 years and was in fact re-enforced in Dodd-Frank and this type of disparate treatment would seem to violate this well-established concept of cross-border supervision.

Third, section 5(c)(3) of the Bank Holding Company Act would appear to be an express statutory provision that prohibits the Federal Reserve from overriding the capital requirements of a functionally regulated subsidiary, such as a broker- dealer subsidy, whose capital requirements are established by the SEC. Under the Fed's proposed rule, it would appear that the IHC approach is merely an artificial artifice, with no statutory basis, to establish a Fed capital requirement on top of SEC's requirements for a foreign-owned broker-dealer. This would seem to directly violate this Bank Holding Company Act provision, particularly in the case of a foreign-owned broker-dealer that has no US bank affiliates.

Finally, sections 165(b)(3) & 165(b)(4) of Dodd-Frank, appear to say that in prescribing prudential standards under 165 that the Fed, should take into account whether a firm

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owns an insured depository institution (Sec.165(B)(3)(ii)), and shall consult with the firm's primary supervisor regarding a functionally regulated subsidiary.(Sec. 165(b)(4)) Again in the case of a foreign owned broker-dealer that is not affiliated with an insured depository institution there is no evidence that the Fed has complied with these express provisions of Dodd-Frank in the rulemaking.

Beyond these specific concerns, it is worth pointing out that during consideration of the Dodd-Frank Act, Congress explicitly addressed how foreign banking organizations should be regulated in the U.S. While Dodd-Frank instructs the Federal Reserve to apply enhanced prudential standards upon banking institutions, both domestic and foreign, Congress expressly maintained a notion of deference to home country supervision for jurisdictions with comparable consolidated supervisory regimes. The current proposal essentially eradicates decades of codified law and regulatory practice in international banking by creating an expansion of Fed power over foreign bank supervision, without any regard for comparable or even more robust home country consolidated supervisory requirements. Any notion that this comparability analysis should only be limited to a foreign branch and does not extend to the broader home country regulation of the consolidated firm is misplaced and would again defy years of practice under the international banking statutes as well as Congressional intent.

Moreover, the proposal may violate the internationally-recognized and codified principle of "national treatment," which prohibits a host country from applying disparate standards to domestic and foreign-owned entities. Under this trade construct, for over 35 years, both U.S. and foreign banks have been evaluated based on their parent company's global capital & liquidity for supervisory purposes. Under GATT/WTO principles and the International Banking Act, the Fed has generally deferred to the home country regulator for capital adequacy of the parent. The current proposal, in requiring a separately capitalized intermediate holding company to be the top U.S.-based entity, applies the enhanced prudential standards across a host of legal organizational entities, including foreign-owned broker dealers, despite the same standards not being applied to domestic-owned broker-dealers.

It is important that the US remain a hospitable place for both domestic and international providers of financial services products, for it is ultimately the consumer that benefits from the choice and competition created by a vibrant and diverse marketplace. As always, thank you for your thoughtful consideration of these matters and I look forward to your reply.

Sincerely,

Spencer Bachus
Member of Congress

Witness Bio
Chairman Mary Jo White

Mary Jo White was sworn in as the 31st Chair of the SEC on April 10, 2013. She was nominated to be SEC Chair by President Barack Obama on Feb. 7, 2013, and confirmed by the U.S. Senate on April 8.

Chairman White arrived at the SEC with decades of experience as a federal prosecutor and securities lawyer. As the U.S. Attorney for the Southern District of New York from 1993 to 2002, she specialized in prosecuting complex securities and financial institution frauds and international terrorism cases. Under her leadership, the office earned convictions against the terrorists responsible for the 1993 bombing of the World Trade Center and the bombings of American embassies in Africa. She is the only woman to hold the top position in the 200-year-plus history of that office.

Prior to becoming the U.S. Attorney for the Southern District of New York, Chairman White served as the First Assistant U.S. Attorney and later Acting U.S. Attorney for the Eastern District of New York from 1990 to 1993. She previously served as an Assistant U.S. Attorney for the Southern District of New York from 1978 to 1981 and became Chief Appellate Attorney of the Criminal Division.

After leaving her U.S. Attorney post, Chairman White became chair of the litigation department at Debevoise & Plimpton in New York, where she led a team of more than 200 lawyers. Chairman White previously was a litigation partner at the firm from 1983 to 1990 and worked as an associate from 1976 to 1978.

Chairman White earned her undergraduate degree, Phi Beta Kappa, from William & Mary in 1970, and her master's degree in psychology from The New School for Social Research in 1971. She earned her law degree in 1974 at Columbia Law School, where she was an officer of the Law Review. She served as a law clerk to the Honorable Marvin E. Frankel of the U.S. District Court for the Southern District of New York.

Chairman White has won numerous awards in recognition of her outstanding work both as a prosecutor and a securities lawyer. The 2012 Chambers USA Women in Law Awards named her Regulatory Lawyer of the Year. Among other honors she has received are the Margaret Brent Women Lawyers of Achievement Award, the George W. Bush Award for Excellence in Counterterrorism, the Sandra Day O'Connor Award for Distinction in Public Service, and the "Women of Power and Influence Award" given by the National Organization for Women.

Chairman White is a fellow in the American College of Trial Lawyers and the International College of Trial Lawyers. She also has served as a director of The NASDAQ Stock Exchange and on its executive, audit, and policy committees. Chairman White is a member of the Council on Foreign Relations.

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

THE CHAIRMAN

November 28, 2011

The Honorable Jack Reed
Chairman
Subcommittee on Securities, Insurance and Investment
Committee on Banking, Housing and Urban Affairs
United States Senate
534 Dirksen Senate Office Building
Washington, DC 20510-3903

Dear Chairman Reed:

Thank you for the recent opportunity for senior staff of the Securities and Exchange Commission to appear before the Subcommittee on Securities Insurance and Investment to discuss our progress regarding management and structural reforms at the agency. During the hearing, our Director of Enforcement identified statutory limitations on our ability to pursue penalties and factors that influence the structure of our settlements. This letter provides additional information regarding these issues, and some suggested legislative solutions.[1]

As you know, the Commission has worked to streamline and strengthen its enforcement program and in so doing has achieved outstanding results. The agency filed a record 735 enforcement actions in fiscal year 2011, including many cases involving highly complex products, transactions, and market practices. More than $2.8 billion in penalties and disgorgement was ordered in Commission enforcement actions in fiscal year 2011. In the area of financial crisis related actions, the Commission has charged more than 80 individuals and entities, including approximately 40 CEOs, CFOs and senior officers.

Notwithstanding these impressive results, the Commission's statutory authority to obtain civil monetary penalties with appropriate deterrent effect is limited in many circumstances. As described below, certain statutory changes would further enhance the effectiveness of the Commission's enforcement program by expanding the Commission's authority to seek monetary penalties for the most serious securities law violations. The changes would increase the statutory limits on civil monetary penalties, more closely link the size of monetary penalties to the scope of harm to investors and associated investor losses, and substantially raise the financial stakes for securities law recidivists.

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[1] The views expressed in this letter are mine and do not necessarily represent the views of the full Commission.

Imposing Appropriate Monetary Penalties for Serious Violations

The federal securities laws authorize the Commission to obtain monetary penalties in both federal court actions and administrative proceedings. These laws generally set forth two alternative methods for calculating the maximum amount of penalties. The first method, applicable in both civil cases and administrative actions, permits a per "violation" calculation, the amount of which increases by tier based on the seriousness of the misconduct. Currently, the highest tier (tier three) – available for violations with the most substantial consequences to investors – is capped by statute at $150,000 per violation for individuals and $725,000 per violation for entities. The second calculation method provided by statute permits imposition of a penalty equal to "the gross amount of pecuniary gain" to the defendant "as a result of the violation." *See* Securities Act of 1933 § 20(d)(2); Securities Exchange Act of 1934 § 21(d)(3)(B); Investment Company Act of 1940 § 42(e)(2); Investment Advisers Act of 1940 § 209(e)(2). This second calculation method can only be used to determine the maximum penalty amount in a federal court action and is not available in administrative proceedings.

In many cases, these provisions impose substantial constraints on the penalties that a court or the Commission can assess because the gross amount of the pecuniary gain to a defendant may be small relative to the seriousness of the violation and the resulting harm to investors. For example, many frauds involving misrepresentation of a public company's financial condition may result in a relatively small pecuniary gain to the company itself or the corporate managers who committed the fraud. Yet such frauds often result in enormous losses to innocent investors. In those cases, the maximum penalty available to the Commission may not adequately reflect the seriousness of the violation or the impact on victims of the fraud.

Three targeted changes would increase the size of the civil penalties available under both existing calculation methods, provide a new calculation method intended to tie the size of a penalty to the amount of associated investor losses, and make the same calculation methods available in both civil and administrative actions.

1. The first proposed statutory change would increase the per violation cap applicable to the most serious violations (*i.e.*, tier three) to $1 million per violation for individuals and $10 million per violation for entities. That would help to ensure that a third tier penalty has an appropriate deterrent effect on both individual and corporate violators, and is not viewed as just a cost of doing business.

2. The second proposed statutory change would amend the maximum tier three penalty to authorize penalties equal to *three times* the "gross amount of pecuniary gain" to the defendant and make a calculation method based on "gross amount of pecuniary gain" available in administrative proceedings for all violations. That would allow the Commission to address situations where the actual pecuniary gain to the violator is relatively small compared to the nature or magnitude of the wrongdoing, and would eliminate the current disparity between the penalty relief available in district court and administrative proceedings.

3. The third proposed statutory change would authorize a calculation method for tier three penalties based on the amount of "investor losses" incurred as a result of a defendant's violation that would be available in both civil and administrative actions. That would allow the Commission to take into account more directly the harm inflicted on investors in seeking appropriate penalties.[2]

Together, these changes would provide the Commission with greater flexibility with regard to monetary penalties in cases where the misconduct is very serious, repeated, or involves substantial investor losses, but the current statutes do not allow for an appropriately significant penalty.

Authorizing Greater Penalties for Recidivists

As the Committee is aware, the Commission sometimes is confronted with individuals or entities that have violated the securities laws repeatedly. In some instances, such defendants' subsequent misconduct violates the federal securities laws and/or a federal court injunction or a bar previously obtained or imposed by the Commission. Current law does not provide the Commission with adequate tools to deter this category of violators. Two statutory changes would provide new sources of penalty authority that would explicitly increase the cost of repeat offenses.

1. The Commission should be authorized to seek a penalty enhancement in the current action equal to three times the otherwise applicable penalty cap if within the preceding five years a defendant has been criminally convicted for securities fraud or become subject to a judgment or order imposing monetary, equitable, or administrative relief in any SEC action alleging fraud. That would enable the Commission to seek monetary penalties against recidivists that are over-and-above the limitations described previously, regardless of the calculation method used.

2. The Commission should be authorized to seek a civil penalty if an individual or entity has violated an existing federal court injunction or a bar obtained or imposed by the Commission. That would include officer and director bars (imposed under Sections 8A(f) or 20(e) of the Securities Act or Sections 21(d)(2) or 21C(f) of the Exchange Act), penny stock bars (imposed under Section 20(g) of the Securities Act or Sections 15(b)(6) or 21(d)(6) of the Exchange Act), and other equitable disqualifications ordered by a court (under Section 21(d)(5) of the Exchange Act). This approach would be more efficient, effective, and flexible than the limited and cumbersome civil contempt remedy. Such authority also would be comparable to the Commission's existing ability to obtain civil penalties for violations of its administrative Cease and Desist orders. *See* Securities Act of 1933 § 20(d)(1); Securities Exchange Act of 1934 § 21(d)(3)(A); Investment Company Act of 1940 § 42(e)(1); Investment Advisers Act of 1940 § 209(e)(1).

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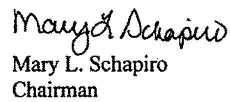
[2] Implementing the change may require the Commission to expend significant additional resources to determine and prove the amount of investor losses in particular cases – for example, to conduct event studies or to retain expert witnesses to evaluate and opine on such losses.

The Honorable Jack Reed
Page 4

<u>Conclusion</u>

The statutory changes proposed above would substantially enhance the effectiveness of the Commission's enforcement program by addressing existing limitations that have resulted in criticism regarding the adequacy of Commission actions against those who violate the securities laws. I have asked my staff to prepare draft legislative language for these five proposals that we will provide shortly under separate cover. We would welcome the opportunity to work with the Subcommittee and its staff to address these limitations on penalty authority by further developing the proposals discussed above.

Sincerely,



Mary L. Schapiro
Chairman

cc: Ranking Member Mike Crapo

Wind farms get pass on bald eagle deaths

May 14, 2013 10:10:27 AM

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CONVERSE COUNTY, Wyo. -- It happens about once a month here, on the barren foothills of one of America's green-energy boomtowns: A soaring golden eagle slams into a wind farm's spinning turbine and falls, mangled and lifeless, to the ground.

Killing these iconic birds is not just an irreplaceable loss for a vulnerable species. It's also a federal crime, a charge that the Obama administration has used to prosecute oil companies when birds drown in their waste pits, and power companies when birds are electrocuted by their power lines.

But the administration has never fined or prosecuted a wind-energy company, even those that flout the law repeatedly. Instead, the government is shielding the industry from liability and helping keep the scope of the deaths secret.

Wind power, a pollution-free energy intended to ease global warming, is a cornerstone of President Barack Obama's energy plan. His administration has championed a $1 billion-a-year tax break to the industry that has nearly doubled the amount of wind power in his first term.

But like the oil industry under President George W. Bush, lobbyists and executives have used their favored status to help steer U.S. energy policy.

The result is a green industry that's allowed to do not-so-green things. It kills protected species with impunity and conceals the environmental consequences of sprawling wind farms.

More than 573,000 birds are killed by the country's wind farms each year, including 83,000 hunting birds such as hawks, falcons and eagles, according to an estimate published in March in the peer-reviewed Wildlife Society Bulletin.

Getting precise figures is impossible because many companies aren't required to disclose how many birds they kill. And when they do, experts say, the data can be unreliable.

When companies voluntarily report deaths, the Obama administration in many cases refuses to make the information public, saying it belongs to the energy companies or that revealing it would expose trade secrets or implicate ongoing enforcement investigations.

Nearly all the birds being killed are protected under federal environmental laws, which prosecutors have used to generate tens of millions of dollars in fines and settlements from businesses, including oil and gas companies, over the past five years.

"We are all responsible for protecting our wildlife, even the largest of corporations," Colorado U.S. Attorney David M. Gaouette said in 2009 when announcing Exxon Mobil had pleaded guilty and would pay $600,000 for killing 85 birds in five states, including Wyoming.

The large death toll at wind farms shows how the renewable energy rush comes with its own environmental consequences, trade-offs the Obama administration is willing to make in the name of cleaner energy.

"It is the rationale that we have to get off of carbon, we have to get off of fossil fuels, that allows them to justify this," said Tom Dougherty, a long-time environmentalist who worked for nearly 20 years for the National Wildlife Federation in the West, until his retirement in 2008. "But at what cost? In this case, the cost is too high."

The Obama administration has refused to accept that cost when the fossil-fuel industry is to blame. The BP oil company was fined $100 million for killing and harming migratory birds during the 2010 Gulf oil spill. And PacifiCorp, which operates coal plants in Wyoming, paid more than $10.5 million in 2009 for electrocuting 232 eagles along power lines and at its substations.

But PacifiCorp also operates wind farms in the state, where at least 20 eagles have been found dead in recent years, according to corporate surveys submitted to the federal government and obtained by The Associated Press. They've neither been fined nor prosecuted. A spokesman for PacifiCorp, which is a subsidiary of MidAmerican Energy Holdings Co. of Des Moines, Iowa, said that's because its turbines may not be to blame.

"What it boils down to is this: If you electrocute an eagle, that is bad, but if you chop it to pieces, that is OK," said Tim Eicher, a former U.S. Fish and Wildlife Service enforcement agent based in Cody, who helped prosecute the PacifiCorp power line case.

By not enforcing the law, the administration provides little incentive for companies to build wind farms where there are fewer birds. And while companies already operating turbines are supposed to avoid killing birds, in reality there's little they can do once the windmills are spinning.

Wind farms are clusters of turbines as tall as 30-story buildings, with spinning rotors the size of jetliners. Though the blades appear to move slowly, they can reach speeds up to 170 mph at the tips, creating tornado-like vortexes.

Flying eagles behave like drivers texting on their cellphones; they don't look up. As they scan for food, they don't notice the industrial turbine blades until it's too late.

The rehabilitation coordinator for the Rocky Mountain Raptor Program, Michael Tincher, said he euthanized two golden eagles found starving and near death near wind farms. Both had injuries he'd never seen before: One of their wings appeared to be twisted off.

"There is nothing in the evolution of eagles that would come near to describing a wind turbine. There has never been an opportunity to adapt to that sort of threat," said Grainger Hunt, an eagle expert who researches the U.S. wind-power industry's deadliest location, a northern California area known as Altamont Pass. Wind farms built there decades ago kill more than 60 per year.

Eagle deaths have forced the Obama administration into a difficult choice between its unbridled support for wind energy and enforcing environmental laws that could slow the industry's growth.

Former Interior Secretary Ken Salazar, in an interview with the AP before his departure, denied any preferential treatment for wind. Interior Department officials said that criminal prosecution, regardless of the industry, is always a "last resort."

"There's still additional work to be done with eagles and other avian species, but we are working on it very hard," Salazar said. "We will get to the right balance."

Meanwhile, the Obama administration has proposed a rule that would give wind-energy companies potentially decades of shelter from prosecution for killing eagles. The regulation is currently under review at the White House.

The proposal, made at the urging of the wind-energy industry, would allow companies to apply for 30-year permits to kill a set number of bald or golden eagles. Previously, companies were only eligible for five-year permits.

In exchange for the longer timetable, companies agree that if they kill more eagles than allowed, the government could require them to make changes. But the administration recently said it would cap how much a company could be forced to spend on finding ways to reduce the number of eagles its facility is killing.

The Obama administration said the longer permit was needed to "facilitate responsible development of renewable energy" while "continuing to protect eagles."

That's because without a long-term authorization to kill eagles, investors are less likely to finance an industry that's violating the law.

Typically, the government would be forced to study the environmental effects of such a regulation before implementing it. In this case, though, the Obama administration avoided a full review, saying the policy was nothing more than an "administrative change."

"It's basically guaranteeing a black box for 30 years, and they're saying 'trust us for oversight.' This is not the path forward," said Katie Umekubo, a renewable energy attorney with the Natural Resources Defense Council and a former lawyer for the Fish and Wildlife Service. In private meetings with industry and government leaders in recent months, environmental groups have argued that the 30-year permit needed an in-depth environmental review.

The tactics have created an unexpected rift between the administration and major environmental groups favoring green energy that, until the eagle rule, had often been on the same side as the wind industry.

Those conservation groups that have been critical of the administration's stance from the start, such as the American Bird Conservancy, have often been cut out of the behind-the-scenes discussions and struggled to obtain information on bird deaths at wind farms.

"There are no seats at the exclusive decision-making table for groups that want the wind industry to be held accountable for the birds it kills," said Kelly Fuller, who works on wind issues for the group.

The eagle rule is not the first time the administration has made concessions for the wind-energy industry.

Last year, over objections from some of its own wildlife investigators and biologists, the Interior Department updated its guidelines and provided more cover for wind companies that violate the law.

The administration and some environmentalists say that was the only way to exact some oversight over an industry that operates almost exclusively on private land and generates no pollution, and therefore is exposed to little environmental regulation.

Under both the Migratory Bird Treaty Act and the Bald and Golden Eagle Protection Act, the death of a single bird without a permit is illegal.

But under the Obama administration's new guidelines, wind-energy companies -- and only wind-energy companies -- are held to a different standard. Their facilities don't face additional scrutiny until they have a "significant adverse impact" on wildlife or habitat. But under both bird protection laws, any impact has to be addressed.

The rare exception for one industry substantially weakened the government's ability to enforce the law and ignited controversy inside the Interior Department.

"U.S. Fish and Wildlife Service does not do this for the electric utility industry or other industries," Kevin Kritz, a government wildlife biologist in the Rocky Mountain region wrote in government records in September 2011. "Other industries will want to be judged on a similar standard."

Experts working for the agency in California and Nevada wrote in government records in June 2011 that the new federal guidelines should be considered as though they were put together by corporations, since they "accommodate the renewable energy industry's proposals, without due accountability."

The Obama administration, however, repeatedly overruled its experts at the Fish and Wildlife Service. In the end, the wind-energy industry, which was part of the committee that drafted and edited the guidelines, got almost everything it wanted.

"Clearly, there was a bias to wind energy in their favor because they are a renewable source of energy, and justifiably so," said Rob Manes, who runs the Kansas office for The Nature Conservancy and who served on the committee. "We need renewable energy in this country."

The government also declared that senior officials in Washington, many of whom are political appointees, must approve any wind-farm prosecution. Normally, law-enforcement agents in the field have the authority to file charges with federal attorneys.

While all big cases are typically cleared through headquarters, such a blanket policy has never been applied to an entire industry, former officials said.

"It's over," Eicher said. "You'll never see a prosecution now."

Not so, says the Fish and Wildlife Service. It said it is investigating 18 bird-death cases involving wind-power facilities, and seven have been referred to the Justice Department. A spokesman for the Justice Department declined to discuss the status of those cases.

Dan Ashe, the Fish and Wildlife Service's director, in an interview Monday with The Associated Press said his agency always made it clear to wind companies that if they kill birds they would still be liable.

"We are not allowing them to do it. They do it," he said of the bird deaths. "And we will successfully prosecute wind companies if they are in significant noncompliance."

But officials acknowledge that their priority is cooperating with companies before wind farms are built to encourage them to be put where they won't harm birds. Once they are built, there is little companies can do except shut down turbines or remove them -- and that means reducing the amount of electricity they generate and violating deals struck with companies purchasing their electricity.

By contrast, there are easy fixes for oil companies and companies operating power lines to stop killing birds. The government often requests companies take such steps before it decides to prosecute.

"We just can't be bringing a criminal case against a company that is up and running if there is not a solution," said Jill Birchell, head of the Fish and Wildlife Service law enforcement office in California and Nevada. "We can fine them, but that doesn't help eagles."

In the meantime, birds continue to die. The golden eagle population in the West, prior to the wind energy boom, was declining so much that the government's conservation goal in 2009 was not to allow the eagle population to decrease by a single bird.

The reason boils down to biology. Eagles take five years to reach the age when they can reproduce, and often they only produce one chick a year.

In its defense, the wind-energy industry points out that more eagles are killed each year by cars, electrocutions and poisoning than by turbines.

Ashe noted that the government doesn't require other industrial facilities to disclose the numbers of birds they kill.

Documents and emails obtained by the AP offer glimpses of the problem: 14 deaths at seven facilities in California, five each in New Mexico and Oregon, one in Washington state and another in Nevada, where an eagle was found with a hole in its neck, exposing the bone.

Unlike the estimates, these are hard numbers, proof of deaths, the beginnings of a mosaic revealing the problem.

One of the deadliest places in the country for golden eagles is Wyoming, where federal officials said wind farms have killed more than four dozen golden eagles since 2009, predominantly in the southeastern part of the state. The officials spoke on condition of anonymity because they were not authorized to disclose the figures.

The Interior Department recently approved construction of the nation's largest wind farm in Wyoming, with what would be 1,000 turbines. The federal government predicts that project, which was analyzed because it was on federal land, would kill 46 to 64 eagles each year.

At a different facility, Duke Energy's Top of the World wind farm, a 17,000-acre site with 110 turbines located about 35 miles east of Casper, 10 eagles have been killed in the first two years of operation. It is the deadliest of Duke's 15 wind power plants for eagles.

The company's environmental director for renewable energy, Tim Hayes, said Duke is doing all it can, not only because it wants to fix the problem but because it could reduce the company's liability. Two of the company's wind farms in Wyoming -- Top of the World and Campbell Hill -- are under investigation by the federal government for the deaths of golden eagles and other birds, according to a report the company filed with the Securities and Exchange Commission last week. The report was filed after the AP visited a Duke facility in Wyoming and asked senior executives about the deaths.

Duke encourages workers to drive slower so as not to scare eagles from their roosts. They remove dead animals that eagles eat. And they've removed rock piles where the bird's prey lives. They also keep internal data on every dead bird in order to determine whether these efforts are working. The company is also testing radar technology to detect eagles and is considering blaring loud noises to prevent the birds from flying into danger.

The only other option is shutting off the turbines when eagles approach. And even that method hasn't been scientifically proven to work.

At Top of the World, Duke shut down 13 turbines for a week in March, often the deadliest time for eagles. The experiment, the company says, paid off. Not a single eagle was killed that month.

Hayes says the company has repeatedly sought a permit from the federal government to kill eagles legally, but was told it was killing too many to qualify.

When an eagle is killed, Duke employees are also prohibited by law from removing the carcass.

Each death is a tiny crime scene. So workers walk out underneath the spinning rotors and cover the dead bird with a tarp. It lies there, protected from scavengers but decaying underneath its shroud, until someone from the government comes to get it.

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THE WALL STREET JOURNAL.
WSJ.com

BUSINESS | August 25, 2011

SEC Bears Down on Fracking

By DEBORAH SOLOMON

WASHINGTON—The Securities and Exchange Commission is asking oil and gas companies to provide it with detailed information—including chemicals used and efforts to minimize environmental impact—about their use of a controversial drilling process used to crack open natural gas trapped in rocks.

Mark Ovaska

A pipeline being assembled near Montrose, PA, on August 25, 2010.

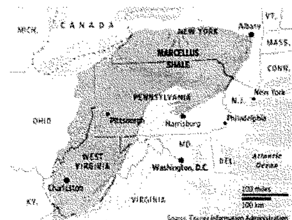
The federal government's investor-and-markets watchdog is stepping into the heated environmental debate surrounding hydraulic fracturing, or "fracking," according to government and industry officials, even as state and federal environmental officials have begun to bring greater pressure on the industry. The process, which involves pumping water, chemicals and sand underground to free difficult-to-reach natural gas in shale basins, has come under criticism from environmental groups ad some lawmakers over concerns toxins in the mix may contaminate air and water.

The SEC move shows the broad interest among Washington regulators in taking a closer look at fracking and suggests companies that are betting billions of dollars on the technology will increasingly need to weigh disclosing techniques they often consider proprietary. Battles over disclosure have already broken out at the state level, including in states such as New York and Pennsylvania that sit on the giant Marcellus Shale, an underground formation that has become a fracking hotbed because of the large quantities of natural gas there. Just last week, Noble Energy Inc. paid $3.4 billion for a stake in developing 663,350 acres there.

Regulators in several states have identified cases in which drilling—although not necessarily the fracturing process in particular—has allowed natural gas to seep into residential water wells, and at least one scientific study has linked drilling and gas contamination more broadly. But there have been few if any documented cases of contamination by the chemicals used in hydraulic fracturing. The industry acknowledges that improperly constructed wells can allow gas to escape, but says such cases are rare and aren't directly tied to fracturing itself.

In the past, the SEC has trained its attention on other areas of concern, such as subprime mortgages and credit-default swaps, and has asked companies to provide additional information to

investors. Government officials said the SEC's interest in fracking is in ensuring investors are being told about risks a company may face related to its operations, such as lawsuits, compliance costs or other uncertainties. Other federal agencies like the Environmental Protection Agency are collecting information about fracking, but those efforts are separate from the SEC.



For the moment, the SEC isn't requiring broad, standardized disclosure of fracking information to the public. Instead, oil and gas companies are being asked by the agency's office that oversees corporate disclosure to supply information confidentially to the SEC, and the agency, in turn, will likely require them to publicly disclose some of that information, according to government officials.

"If there's something in [a company's] field of operation that creates uncertainty, that's something they may want to talk about" with investors, said a government official.

The SEC's requests drew criticism from some in the industry about potential regulatory overkill.

"While our industry absolutely supports common sense disclosure and transparency measures, such duplicative inquires that may fall outside of an agency's core mission, are troubling and counter to what our nation needs at this time," said Kathryn Klaber, president of Marcellus Shale Coalition, an industry group.

An SEC spokesman said "in the course of our filing reviews staff will ask questions related to the areas disclosed in the company's filings." The EPA didn't respond to requests for comment.

The SEC's foray into the issue comes as the Obama administration is trying to find a middle ground between environmental concerns over fracking and an industry that is creating jobs and increasing domestic supplies of an alternative energy source to coal. Natural gas currently provides about 25% of total U.S. energy and is projected to increase to 45% by 2035, according to the U.S. Energy Information Administration. In addition to a fracking study being conducted by the EPA, the Department of Energy and the Interior Department have also been examining the practice. Some states have fined drilling companies for environmental problems.

For securities regulators, two recent energy-related disasters are fresh in their minds: the crippling of Tokyo Electric Power Co.'s Fukushima Daiichi nuclear-power plant in March and last year's BP PLC oil spill in the Gulf of Mexico. In both cases, some investors were surprised at the risk to which the companies were exposed, and their share prices fell sharply.

The SEC's questions in recent letters include which chemicals are being injected into the ground, what companies are doing to minimize water usage and what steps they are taking to minimize environmental impact, according to copies reviewed by The Wall Street Journal.

The questions are already prompting some companies to disclose more. SandRidge Energy, a small, Oklahoma company, beefed up disclosure related to fracking operations after the SEC asked a series of questions in connection with a public offering of a trust SandRidge completed last week. For instance, the company said in a recent financial filing that its fracking fluid contains 99% fresh water, and the remainder includes the food additive guar, enzymes and other chemicals, which it didn't name.

Fracking fluids include some toxic chemicals, based on company disclosures of chemicals such as benzene and formaldehyde for congressional reports and at voluntary disclosure sites.

Kevin White, senior vice president of SandRidge, said "responding to those comments would be easier than what other companies might face" because the firm doesn't use many chemicals in its fracking fluid.

Industry representatives said much depends on how specific the SEC wants companies to be and cautioned they would resist revealing proprietary information.

"While we support disclosing our ingredients, it is critical to our business that we protect our proprietary information, including the recipes of our products," said spokeswoman Tara Mullee Agard of Halliburton Co., one of the largest providers of hydraulic-fracturing services to the energy industry.

Already some companies have said they will voluntarily publicize their chemicals online at FracFocus.org, and several states, including Wyoming, Texas and Arkansas, have recently passed mandatory disclosure rules. The companies will make the information public through state registries.

Fracking is primarily regulated by states and is largely exempt from some federal statutes, such as the Safe Water Drinking Act. The EPA's study on whether fracking affects drinking water is to be released at the end of 2012. For the study, nine companies provided information on the chemicals they use after an agency request last year.

The SEC has also been investigating whether companies are overstating the long-term productivity of their natural-gas wells and has issued subpoenas to at least two firms, according to company financial disclosures earlier this month. The agency subpoenaed Quicksilver Resources Inc. and ExCo Resources Inc. The New York attorney general's office, meanwhile, has also issued subpoenas this month to various companies, including Range Resources Corp., Goodrich Petroleum Corp. and Cabot Oil & Gas Corp., over their estimates.

Jim Smith, a partner at Houston law firm Porter Hedges LLP specializing in environmental law, questioned whether the type of fracking information the SEC is requesting is material to a company. "I have not heard of companies in relatively recent times having significant environmental liabilities associated with hydraulic fracturing that in any way affected their reported worth," he said.

Investors, including the $129.4 billion New York State Common Retirement Fund, have begun agitating for enhanced disclosure of fracking operations over the past few years and have successfully included shareholder proposals at 16 companies. Though none have passed, proponents at Chevron Corp. got 41% support, backers at Exxon Mobil Corp. got 28% and Williams Cos. holders got 42%. Some companies, such as Williams and Cabot, have increased disclosure of their fracking operations as a result of the proposals.

New York State Comptroller Thomas P. DiNapoli, who runs the New York State Common Retirement Fund, said some companies drilling in the Marcellus Shale in Pennsylvania have had to pay large fines and suffered reputational damage over fracking problems. Chesapeake Energy and Cabot have paid fines there. "Only through appropriate disclosure do you get the information you need to make informed and sound investment decisions," he said.

—Daniel Gilbert and Russell Gold contributed to this article.

Questions for the Record for SEC Chair Mary Jo White
Hearing on Oversight of the SEC's Agenda, Operations, and FY 2014 Budget Request
House Financial Services Committee
May 16, 2013

Representative Bill Huizenga

Pay Ratio

1. **The Federal securities laws already require public companies to disclose comprehensive data on annual compensation. Section 953(b) of the Dodd-Frank Act directs the SEC to write rules that would require public companies to compute the ratio of the median annual compensation of all of its employees to the annual total compensation of the CEO. Are the mandates of Section 953(b) really necessary to enhance the existing executive compensation disclosures? Is the data required to be computed and disclosed in Section 953(b) material to investors? Why or why not?**

2. **The provisions in Section 953 of the Dodd-Frank Act have been cited by some as a "logistical nightmare" because of the multitude of factors that a company must consider when calculating total compensation. What factors do you believe must be considered by an issuer to determine this calculation? Would transit benefits or employer-paid health care costs be a component of compensation? Should domestic and all multinational employees be a part of this calculation? What about part-time employees or independent contractors? Would you agree that the statute is very vague?**

3. **It would appear that the pay ratio will be difficult and costly for issuers to implement, especially large global issuers with operations in dozens of countries. According to a Center On Executive Compensation survey, a majority of large employers estimated it would require at least three months (in some cases longer) to gather and calculate the pay ratio for inclusion in the proxy. What steps has the Commission staff taken to identify the costs of implementation?**

4. **Do you think the benefit, if any, of the pay ratio disclosure is worth the cost to companies, especially those with large global workforces that will have to spend significant amounts to gather the data or develop systems to do so?**

   Response: As a general matter, completing the rulemakings mandated by both the Dodd-Frank Act and the JOBS Act is a priority for me, including implementing Section 953(b) of the Dodd-Frank Act. The staff is actively working on developing recommendations for the Commission concerning implementation of Section 953(b). In doing so, the staff has met with numerous interested groups and has received a great deal of information.

   This rulemaking is challenging and raises a number of new issues for the Commission and registrants that require careful consideration, including the questions you identified regarding implementation and the potential costs and benefits associated with the

requirements. As evidenced in the public comment file available on the Commission's website, which includes more than 20,000 comment letters relating to this rulemaking, this is an area where people have strong views. As you are aware, some commenters have raised questions regarding the usefulness to investors of the mandated disclosures and the ability of companies to collect the data necessary to make the required disclosures. Those commenters also have asserted that the compliance costs will be quite high. In contrast, others argue that the disclosures required by Section 953(b) represent critically important information for investors and have expressed concerns about any implementation approach that would narrow the provision's scope.

Section 953(b) requires the Commission to amend its rules to require disclosure of the ratio of the median annual total compensation of all employees of the issuer and the CEO's annual total compensation. Specifically, the provision requires that total compensation be calculated under the Commission's executive compensation rules that were in effect the day before the enactment date of the Dodd-Frank Act. The definition of "total compensation" used in those executive compensation rules is complex and different from other definitions of compensation that are used for accounting and tax purposes.

In addressing these issues, as with all of the Commission's rulemaking, I believe that rigorous economic analysis is important and should inform and guide our decisions. Our analysis of these issues, and the potential economic impacts of the legislative changes and the associated rules, are ongoing and will be reflected in the proposing release. In addition, we look forward to receiving public comment on the proposal, particularly with respect to the potential costs and benefits of the disclosure.

M&A Brokers

1. **A proposal to "right-size" federal regulation of merger and acquisition (M&A) intermediaries and business brokers has been among the top recommendations in the 2005, 2006, 2007, 2008, 2009, 2010, and 2011 Government-Industry Forum on Small Business Capital Formation annually hosted by the SEC.**

    - **Do you see this as an important small business capital formation concern?**
    - **Under your leadership, what priority will be given to this small business issue?**

    Response: The Commission and its staff have taken this issue very seriously. In 2006, the staff in the Division of Trading and Markets' Office of Chief Counsel (TM-Chief Counsel) issued a no-action letter to Country Business, Inc. building upon guidelines it had previously issued to International Business Exchange Corporation. Those letters identify a range of business broker activities in which an intermediary may engage without being required to register as a broker-dealer. I understand that companies and intermediaries are interested in receiving updated guidelines, as business practices have evolved over the years. I am receptive to these requests. TM-Chief Counsel staff have met with interested parties, as well as the state securities regulators and the Financial

Industry Regulatory Authority (FINRA), to gather a variety of viewpoints and discuss these issues with the goal of developing updated guidance.

2. **One of the major obstacles to the growth of small businesses has been the dwindling number of broker-dealers willing to handle smaller offerings given the cost of due diligence and their risks to subsequent liability. In 2005 the American Bar Association's Private Placement Broker Task Force and the SEC-hosted Government-Industry Forum on Small Business Capital Formation have since 2005 annually recommended that we simply registration for a classification of broker-dealers that will only engage in private offerings. Presently broker-dealer registration is a "one size fits all" approach and 90% of the requirements are irrelevant to a broker-dealer engaging in limited capital-raising activities. The SEC staff has acknowledged this small business concern but the Commission has not yet addressed it.**

    - **Do you see this as an important small business capital formation concern?**
    - **What do you anticipate the Commission doing to address this issue?**

    Response: A core component of our mission is to facilitate capital formation, and that mission requires us to consider carefully how our rules and regulations impact small businesses. I recognize that a "one size fits all" regulatory scheme may not be the most appropriate one for today's securities market professionals. The standards established by Congress and the Commission for registered broker-dealers are intended to protect both investors and the securities markets. One important question involves what aspects of the broker registration process or the regulations applicable to brokers are or are not appropriate for paid intermediaries who seek to help small businesses sell securities to investors. Any actions taken in this area must also be fully consistent with investor protection.

    The passage of the JOBS Act and the development of a crowdfunding regulatory regime present an opportunity for addressing this issue. Although funding portals will not be required to register with the Commission as broker-dealers, they nevertheless must register as funding portals with the Commission and become members of a registered national securities association. In this regard, FINRA must consider which rules should apply to the limited activities of funding portal members. Currently, staff in our Division of Trading and Markets is working with FINRA to review its rulebook and determine what types of rules should apply to funding portals. This assessment and the resulting regime could serve as a useful predicate for other types of funding intermediaries.

Representative Carolyn McCarthy

As a senior Member of both the Committees on Education and Workforce and Financial Services, I have been deeply invested in the Department of Labor's efforts to redefine the definition of fiduciary for the purposes of ERISA. I have expressed concerns to both the SEC and DOL for their apparent lack of coordination on this effort to avoid duplicative, overlapping or conflicting regulatory environments for entities that provide retirement services.

In March, the SEC issued an approximately seventy page request for information (RFI) seeking input on whether to make new rules about the standards of conduct and regulatory obligations for broker-dealers and investment advisers when they provide personalized investment advice about securities to retail customers. Never once in that RFI is there an indication of coordination with the Department of Labor.

There are concerns from stakeholders in the retirement world that they will have to change procedures twice once for the Department of Labor, who admittedly is moving quicker than the SEC on fiduciary standard, and then again for whenever the SEC provides their guidance. Might I remind you that customer confusion was a large factor underlying both Congress' and the SEC's interest in a uniform fiduciary standard. Yet, if the SEC and DOL fail to coordinate their rules a vast confusion will be created for retail customers. I know I have seen form letters addressed back and forth between your two agencies, but what assurances do we, in Congress, have that you all are working together? Moreover, what kind of timeline is the SEC working on to address standards of conduct?

Response: I appreciate the concerns that you expressed about the potential fiduciary rulemaking by the SEC and that of the Department of Labor. As you note, the SEC has issued an information request regarding a possible uniform fiduciary standard for broker-dealers and investment advisers. The comment period for the request for information ended July 5, 2013.

The Commission made clear in its release that we have not yet determined whether to propose a uniform fiduciary duty for broker-dealers and investment advisers.

My staff informs me that, since the Department of Labor's proposal in 2010, they have coordinated, and continue to coordinate, with Department of Labor staff on the question of how to implement a fiduciary standard and the practical effect for financial services providers – particularly broker-dealers – of operating under a fiduciary standard of conduct, as well as any impact it may have on retail investors. I am committed to continuing this coordination, and I have personally met with leadership from the Department of Labor. I have also directed staff to continue to promote close coordination with their counterparts at the Department of Labor as each agency moves forward with potential rulemaking.

A primary issue that I will be focused on is the prospect of the Department of Labor redefining the fiduciary duty standards for IRA accounts, where broker-dealers routinely interact with retail investors, and how such standards may interact with any fiduciary standard for broker-dealers that the Commission may implement. While it is true that the Department of Labor has its own perspectives, jurisdiction, and statutory authority, my goal and that of the SEC's staff is to continue to coordinate with the Department of Labor as much as is appropriate given our different statutory standards, with the goal of protecting investors without imposing unnecessary or burdensome costs on industry.

Representative Patrick E. Murphy

In order to jumpstart investment in small businesses, the SEC should consider providing relief, where appropriate, to small businesses. Would you agree that shortening Rule 144's required holding period to 3 months for smaller reporting companies would make purchasing "restricted securities" issued by these companies more attractive for investors?

Response: The holding period of Rule 144, which is a safe harbor for the Securities Act Section 4(1) statutory exemption from registration, is a criterion established to demonstrate that the selling security holder did not acquire the securities to be sold under Rule 144 with the intent to distribute the securities to the public. The holding period should be long enough to provide a reasonable indication that an investor has assumed the economic risk of investment in the securities to be resold under Rule 144. The holding period is not intended to impose any unnecessary costs or restrictions on capital formation.

To that end, the Commission reviewed and revised the holding period requirement of Rule 144 several times since its adoption in 1972. In 2007, the Commission substantially shortened the holding period for restricted securities of reporting companies to six months. At the time, I understand that the Commission considered the suggestion from a commenter that the holding period should be shortened to three months, but concluded that, based on its observation of the operation of the rule, a six-month holding period would provide a reasonable indication that an investor has assumed the economic risk of investments in the securities to be resold. Most commenters agreed, noting that a holding period of six months for restricted securities of reporting issuers would increase the liquidity of privately-sold securities and decrease the cost of capital for reporting companies while still being consistent with investor protection.

I believe that the Commission should continue to be mindful of possible need for further changes to the holding period. That said, because the JOBS Act significantly altered the regulatory framework for capital-raising and reporting by smaller companies, in my view it would be best to first implement the JOBS Act and assess its impact before shortening the holding period of Rule 144 even further.

House Financial Services Committee
Hearing on Oversight of the Securities and Exchange Commission

Responses to Questions Submitted By

Congressman Stevan Pearce

Will the SEC continue to ask energy companies to disclose information relating to hydraulic fracturing?

RESPONSE: Staff has advised me that the Division of Corporation Finance is not generally issuing any comments concerning specific information on the nature and extent of the potential environmental impact of hydraulic fracturing operations. If it appears that operational aspects of a company's hydraulic fracturing operations may present a material risk to a company's business, results, or operations that is not disclosed in its filings, the staff may ask the company for analysis or to consider potential modifications to its risk factor disclosure. This approach is consistent with the approach that the staff takes in connection with an assessment of any business risk faced by a company. The goal of the Division's disclosure review program is to enhance investor protection through full and fair disclosure. The disclosure review program is not intended to promote or discourage any particular business activities.

Has the SEC considered asking alternative energy companies to disclose their environmental impact statements?

RESPONSE: No. I understand from the Division of Corporation Finance that in reviewing the disclosures of companies engaged in alternative or traditional production of energy, the staff often finds that these companies disclose the financial and business risks of compliance with federal, state, local, and foreign environmental laws. Some companies provide disclosure about environmental impact statements. Where a company does provide such a statement, I understand any questions the staff might ask would be to enhance risk factor disclosure or management's discussion and analysis disclosure about material costs or risks to the company and/or the potential ramifications to the company if the findings in the statement resulted or may result in the termination of any pending project. The Division's review of a company's disclosure is focused on material costs and risks regarding compliance with environmental regulations and the material costs of remediation where appropriate.

Has the SEC asked alternative energy companies with wind turbines to disclose the number and species of birds that are killed by their turbines?

RESPONSE: No. The Division of Corporation Finance staff has reviewed the disclosures of companies engaged in alternative energy with wind turbines and this issue does not appear to rise to the level of a material factor or risk to a company's business, results, or operations such that disclosure would be required to be provided under our requirements. For many large manufacturers of wind turbines who file reports with the SEC, the portion of a company's business, results, operations, and risks that are attributed to wind turbine manufacturing is generally considered to be not material when considered in the context of the entire reporting company.

<u>Representative Steve Stivers</u>

Municipal Advisors

1.) Section 975 of the Dodd-Frank Act includes provisions to regulate municipal advisors, who were wholly unregulated before Dodd-Frank. It has been nearly three years since Dodd-Frank was enacted, and the SEC has yet to finalize the rule establishing the definition of municipal advisors. These entities remain largely unregulated, creating risks for investors and for state and local governments.

- **When can we expect that the SEC will finalize its municipal advisor rule?**

<u>Response</u>: Finalizing the rules for the registration of municipal advisors is the highest immediate priority project in the Commission's Office of Municipal Securities, and a priority of mine. I will continue to work closely with the Commission in an effort to proceed as promptly as possible to finalize these important rules on municipal advisors.

2.) The municipal advisor provisions in Dodd-Frank are intended to cover previously unregulated entities that advise states and localities as fiduciaries. The SEC's December 2010 proposed advisor rule would go far beyond that, covering entities and activities which Congress never intended. SEC commissioners and staff have indicated that the most egregious over-stepping in the proposed rule will be corrected in the final rule. However, many questions remain unanswered.

- **How, for example, will the SEC's final rule handle the "underwriter exception" to the municipal advisor definition?**

<u>Response</u>: The Commission has received more than 1,000 comments on its proposed municipal advisor registration rules. Many commenters expressed concerns that the proposed rules were overbroad, including with respect to their potential impact on activities of broker-dealers serving as underwriters on the issuance of municipal securities for purposes of the underwriter exception to municipal advisor registration. In addition to reviewing comment letters from bond underwriter groups, the staff also met with several groups representing bond underwriters to discuss their concerns relating to the proposed rules. In developing recommendations for the Commission, the staff is carefully weighing these comments and concerns. We recognize the important role that bond underwriters play in assisting municipalities in the issuance and sale of municipal securities. I anticipate that the final rules will address carefully, among other things, the concerns about overbreadth, including the concerns about the scope of the underwriter exception, and will require appropriate registration of municipal advisors without unnecessarily imposing additional regulation.

3.) This Committee last year unanimously approved legislation which I have introduced with Rep. Moore that would clarify the Dodd-Frank language with respect to municipal advisors. The House passed the bill by voice vote.

- **Will the SEC's final municipal advisor rule be consistent with the bipartisan legislation the House passed last year?**

Response: I appreciate that the general theme underlying this legislation reflects a response to concerns that the SEC's proposed rules in 2010 were overly broad. The staff is developing recommendations for the final rules that I expect will address concerns about overbreadth in a balanced way. Any effort to calibrate the municipal advisor definition, whether at the SEC or through legislation, must strike an appropriate balance. Just as overbreadth is a concern, so too would be rules or legislation that are too narrow in their determinations of who should have to register as municipal advisors, which could undermine the core purposes of this provision. Congress added the municipal advisor provisions to protect municipalities, their taxpayers, and municipal securities investors against conflicted advice and unregulated advisors. These people deserve the benefit of effective municipal advisor regulation.

Private Equity Regulations

Dodd-Frank imposed requirement on Private Equity Funds to Register with the SEC under the Investment Advisers Act

1.) Chairman White, the principal intent of Dodd-Frank was to impose greater regulation on those institutions that posed a significant risk to our financial institutions – while not causing undue harm to American businesses. Under Dodd-Frank, U.S. private equity funds that have at least $150 million of assets under management are now obligated to register with the SEC as investment advisers despite the fact that private-equity funds, in particular middle market growth and buyout funds, have not been shown to contribute to systemic risk of the global financial system. In fact, unlike hedge funds that engage in proprietary trading, PE Funds are structured and operate in a way that is almost identical to venture capital funds, which under Dodd-Frank are exempted from having to register under the Investment Advisers Act. As investment advisors, registration has caused funds to change the manner in which they operate in ways that are not meaningful or protective to investors and has caused these funds, particularly small portfolios, to incur significant costs to comply with the registration requirements. This diverts resources that could otherwise be spent to help portfolio companies grow.

- **Would you support legislation that would exempt private equity fund advisers from registration with the SEC, similar to venture capital funds which have already been exempted from this burdensome regulation?**

Response: Title IV of the Dodd-Frank Act required that advisers to private equity funds with assets under management of $150 million or more register with the Commission. As a result, the Act provides investors with the additional protections registration affords when a private equity fund adviser is managing a significant amount of money. Although private equity funds were not an underlying cause of the recent financial crisis, private equity fund advisers represent a significant and influential part of the financial landscape.

In my view, our markets would not be well-served by narrowing the scope of the Commission's jurisdiction and oversight of these advisers.

Advisers Act registration serves to protect advisory clients from conflicts and other risks associated with clients entrusting their assets to advisers, and the application of these protections should not vary based on an adviser's particular investment strategy. To base exemptions from registration on investment strategy or leverage would result in the securities laws generally favoring or disfavoring particular strategies, which should be avoided when the objective is a fair and level playing field.

Registration under the Advisers Act also provides the SEC with tools to discover and prevent frauds and other violations of the securities laws, including the ability to regularly examine registered advisers, which enhances confidence in our capital markets and promotes fair dealing. Private equity is not immune to fraud. As with other types of funds and advisers, the Commission has brought cases involving private equity funds and their advisory personnel involving unlawful pay to play schemes, insider trading, conflicts of interest, valuation, and misappropriation of assets. It is important, therefore, that we have an appropriate level of oversight of these entities, both for investor protection and market efficiency purposes.

In certain instances, however, it may make sense for the Commission to apply the Advisers Act to private equity fund advisers differently. For example, the Commission adopted different reporting requirements on Form PF based on the size and type of fund. The staff of the Division of Investment Management is engaged in ongoing discussions with various representatives of the private equity industry concerning interpretive and other issues that have arisen as a result of the new registration requirement applicable to private equity and many other private fund advisers.

2.) **As it currently stands, private-equity advisors registered with the SEC must now submit Form PF annually 120 days after the end of the fiscal year. Many of the questions on Form PF are subjective and lack guidance on interpretation. The form was written for firms that trade public securities not firms that make control and non-control investments in middle-market private companies and do not trade or sell these securities except when they exit the investment which is generally four to six years later. The Form PF which was not designed for private equity addresses the fact that this kind of regulation is not relevant for PE Funds.**
Moreover, compliance costs disproportionately impact private equity firms with smaller funds. This will cause some of these firms to close shop. Smaller private equity groups tend to invest in small and middle market companies. An in intended consequence of PF compliance may well be fewer investments in smaller companies.

- **Would you support modifications to Form PF?**

Response: Form PF must be completed by investment advisers that are registered with the SEC or the CFTC, manage one or more private funds, and that, collectively, have at least $150 million in private fund assets under management.

In adopting Form PF, the Commission reduced the scope of required reporting by private equity fund advisers to better take into account the private equity fund business model. The section of Form PF that is completed by advisers with $2 billion or more in private equity fund assets under management generally requests basic information that is tailored to the activities of private equity funds. Private equity fund advisers with less than $2 billion in private equity fund assets under management are not required to complete this specialized section and only complete part 1, which is the general overview part of the Form PF. In addition, large private equity advises are only required to file Form PF once a year, while large hedge fund advisers are required to file quarterly due to the more frequent turnover of their portfolios.

The Commission is sensitive to the costs and benefits of its regulatory requirements and has tried to tailor requirements appropriately. We will continue to strive to identify ways to improve our regulatory requirements without sacrificing investor protection.

3.) **Moreover, middle-market private equity firms typically invest in privately-held companies, the shares of which are not registered under the Securities Act of 1933 and are not publicly traded. Under GAAP accounting standards, when a fund's financial statements are audited by its independent outside auditors, the auditors generally examine the share certificates to confirm that the Fund has possession of them. Under the SEC's Custody Rule Section 206(4)-2, private-equity funds now have to use a registered custodian, which has been estimated to cost as much as $50,000 per year. Again, this obligation was designed for those firms that trade on a regular basis and have no application to private equity funds. Yet, private equity funds have to comply.**

- **Would you support modifications to the Custody Rule with respect to private-equity funds and securities?**

Response: The custody rule was amended in 2009 after the Commission had brought several high profile enforcement actions against investment advisers and broker-dealers alleging fraudulent conduct, including misappropriation or other misuse of investor assets. A private equity fund adviser typically has custody of client assets as a result of serving, or having a related person serve, as the general partner of a client that is a private equity fund, thereby granting the adviser authority to hold client funds or securities. Both the risks to investors in this arrangement, as well as the protections provided by the custody rule, are significant.

The staff and I understand, however, that it may make sense for the Commission to apply the Advisers Act to advisers differently based on the characteristics of the advisers and investments that pose different risks. In light of the Dodd-Frank Act registration requirements and the substantial increase in the number of private equity fund advisers registered with the Commission, the staff of the Division of Investment Management has engaged in ongoing discussions with various representatives of advisers to private funds, including private equity fund advisers, concerning the requirements of the Advisers Act and its rules. This review is in its early stages, but the requirements of the custody rule

are being assessed as part of this effort, including the existing exemption for privately offered securities that permits advisers to not use a qualified custodian to maintain certain non-public securities.

Volcker Rule Parity with SBIC Companies

1.) Chairman White, as you know, the SEC is currently grappling with drafting rules for the implementation of the Volcker Rule, which is very complex. With certain limited exceptions, the draft rule which prohibits banks from investing in private equity funds, contains a carve-out to permit banks to invest in Small Business Investment Companies (SBIC). There are hundreds of other middle-market private equity funds that like SBICs invest in or lend to U.S. small and mid-sized businesses but are not in the SBIC program.

- **Would you support a similar carve-out from the Volcker Rule for private equity funds that are invested in lower and middle market companies? (Investments of under $500 million)**

Response: The treatment of middle market private equity funds in the proposed rule implementing Section 619 of the Dodd-Frank Act (the Volcker Rule) is an issue that has been raised by several commenters. The issue arises because Section 619 provides that a banking entity may not sponsor or invest in, or have certain other business relationships with, a hedge fund or private equity fund. In Section 619, Congress specifically defined hedge funds and private equity funds as issuers that would be investment companies under the Investment Company Act of 1940, but for Section 3(c)(1) or 3(c)(7).

The proposed rule adhered closely to the statutory language in defining a "covered fund" (*i.e.*, a fund subject to the implementing rule) by reference to sections 3(c)(1) and 3(c)(7) of the Investment Company Act, exemptions that commonly are used by hedge funds and private equity funds, as well as other types of investment vehicles, to avoid regulation under that Act. Many commenters have noted that this definition of "covered fund" would include many more types of vehicles than the hedge funds and private equity funds that are specifically referenced in the statute and that many commenters believe should be the main focus of the Volcker Rule prohibitions.

In Section 619, unlike other provisions of Dodd-Frank, Congress did not provide any exemption relating to middle market private equity funds and instead only provided a very limited exemption for "investments in one or more small business investment companies, as defined in section 102 of the Small Business Investment Act of 1958 (15 U.S.C. 662) (SBICs). Consistent with this statutory exemption, the proposed rule would permit banking entities also to *sponsor* any such SBIC.

Our staff continues to work closely with staff from the banking agencies and the CFTC to determine whether the proposed definition can or should be refined and whether it would be appropriate to exempt any additional entities or funds in light of the statute and its goals, including Section 619's provision that the agencies may exempt any activity from

the implementing rule upon a finding that such activity would promote and protect the safety and soundness of banking entities.

Private Equity Managers Register as Broker-Dealers

1.) **Recently, several of the senior staff at the Commission have indicated the Commission intends to focus some of its regulatory efforts on general partners who earn fees in connection with a sale of a portfolio company. Further, we understand that the SEC's concern is where the transaction-based compensation may provide an incentive to the advisor that raises fiduciary duty and conflicts of interest issues and the potential requirement for fund managers who receive compensation to be regulated as a broker-dealer unless the fees they receive are offset against their management fees. It appears that the only reason the SEC is requiring registration is that the General Partner will be receiving a fee that is not being offset against its management fee.**

- **Please comment on the nature of the protections that this registration would provide?**

<u>Response</u>: Broker-dealer oversight provides many important protections to investors. Among other things, it promotes principles of fairness, transparency and financial responsibility, all of which benefit those who do business with broker-dealers. It also addresses the conflicts of interest that can be associated with the receipt of a success fee for a securities transaction. Generally, any person that is "engaged in the business of effecting transactions in securities for the account of others" is required to register as a broker-dealer under the Securities Exchange Act of 1934. Receiving compensation based on the success of a securities transaction is one hallmark of being a broker-dealer.

During examinations of advisers, including the examination of private equity fund advisers newly subject to SEC registration, the staff has observed that some advisers may be receiving transaction-based compensation from portfolio companies for traditional investment banking activities, including negotiation and solicitation services relating to the acquisition, disposition, and recapitalization of portfolio companies. The receipt of compensation in connection with these activities raises the question of whether they extend beyond the traditional investment advisory relationship. The staff has been exploring these issues with representatives of the private equity fund community. That work is ongoing.

2.) **In addition, for more than 25 years, business brokers have been advising business owners with respect to the sale of small businesses. It is the SEC's position that these small business brokers are required to register under the Securities Exchange Act of 1934. A registration requirement here would be cost prohibitive and would, in all likelihood force many of them out of business.**

- **Please indicate the nature of the protections that this registration would provide?**

Response: Because of the broker-dealer's role as an intermediary between customers and the securities markets, broker-dealer registration is a cornerstone of the framework of U.S. securities market regulation. The standards established by Congress and the Commission for registered broker-dealers are intended to protect both investors and the securities markets.

For example, broker-dealers, in addition to the general antifraud provisions of the federal securities laws, are also subject to special anti-fraud rules,[1] have special duties to their customers,[2] must supervise their associated persons,[3] are subject to the Commission's broad disciplinary authority,[4] and are required to be members of an SRO.[5] Broker-dealer registration also provides the markets with a degree of legal certainty. In particular, the use of an unregistered intermediary may taint an offering and potentially create a basis for rescission.[6]

At the same time, I am cognizant of the costs associated with registration, and the unique and limited nature of a business broker's securities activities. In 2006, the staff in the Division of Trading and Markets' Office of Chief Counsel (TM-Chief Counsel) issued a no-action letter to Country Business, Inc., building upon guidelines it had previously issued to International Business Exchange Corporation. Those no-action letters identify a range of business broker activities in which an intermediary may engage without being required to register as a broker-dealer, and the TM-Chief Counsel staff considers issuing further guidance in this area a top priority.

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1 See Section 15(c) of the Exchange Act, and the rules thereunder.

2 See, e.g., Hanly v. SEC, 415 F.2d 589, 596 (2d Cir. 1969) ("A securities dealer occupies a special relationship to a buyer of securities in that by his position he implicitly represents he has an adequate basis for the opinions he renders").

3 See Section 15(b)(4)(E) of the Exchange Act.

4 See Sections 15(c) and 21 of the Exchange Act.

5 See Section 15(b)(8) of the Exchange Act.

6 See Section 29(b) of the Exchange Act; Regional Properties, Inc. v. Financial & Real Estate Consulting Co., 678 F.2d 552, 558 (5th Cir. 1982), aff'd on other grounds, 752 F.2d 178 (5th Cir. 1985) (later appeal); Eastside Church of Christ v. National Plan, Inc., 391 F.2d 357 (5th Cir.), cert. denied, 393 U.S. 913 (1968) (allowing investors to rescind transactions with unregistered broker-dealer).

Insert for the hearing record page 27, line 639:

After the hearing, I inquired of staff at the agency, and no one was aware of any contact from OMB expressing an interest in seeing the potential rulemaking regarding political reporting moved forward.

Insert for the record on page 119, line 2823 of hearing transcript:

During the hearing, Representative Hultgren asked about the current practice of SROs with respect to consideration of economic analysis. With respect to proposed rule changes, each SRO is required to explain the rationale and impact of each proposed rule change filed, which includes a discussion of the potential impact of the applicable rule change on competition.

The notice and comment process under Section 19(b) of the Exchange Act allows for consideration of potential impacts of an SRO's proposed rule change, including concerns raised by commenters about potential economic effects.

Section 3(f) of the Exchange Act provides that whenever the SEC is engaged either in its own rulemaking or in the review of a rule of a self-regulatory organization "and is required to consider or determine whether an action is necessary or appropriate in the public interest," it shall also consider, "in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation."

Representative Hultgren also asked about the current practice of FINRA when administering its other operations, such as its exam and inspection programs, with respect to consideration of economic analysis. While a formal requirement to conduct an economic analysis does not necessarily apply to FINRA's operations, it is my understanding that its examination program is risk-based, in that the scope, content, frequency, and nature of an individual examination will depend on the operational and risk characteristics associated with a particular firm. Specifically, while FINRA takes into account a number of factors when determining when and how often to examine a firm, it pays particular attention to, among other things, a firm's size, business model and product line, including the types of risks associated with particular kinds of products and investment strategies, as well as the percentage of a firm's business that is customer-facing and the regulatory history of a firm and its employees and principals.

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