



Oversight of the Securities
and Exchange Commission

Senate Banking Committee

November 17, 2020

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This is an executive summary of the Senate Banking Committee hearing titled “Oversight of the Securities and Exchange Commission” that occurred on November 17, 2020.

Opening Statements

Chairman Crapo (R-ID) stated that the SEC has taken many important steps to limit economic shocks to the market and used tools like limit bound circuit breaks. Crapo believed that the current mechanisms have served their purpose. He commended Clayton for pursuing additional enforcement actions during the pandemic and for Clayton’s efforts to advance his regulatory agenda like modernizing the exempt offering framework, improved readability for S-K disclosures, and Regulation Best Interest.

Ranking Member Brown (D-OH) remarked that it is time to turn the page on this failed Administration and build an economy that works for everyone. He thanked Clayton for his work on the SECs response to COVID and his efforts to help working families. He encouraged the SEC to do better and make markets work for working people. Brown was worried not only about Clayton’s agenda but advancing one bad rule after another in favor of private interests. He hoped to reverse Clayton’s agenda in the future.

Witness Statement

The Honorable Jay Clayton, Chairman, U.S. Securities and Exchange Commission, stated that while the pandemic significantly impacted how the SEC did its work, it did not affect the work itself. He continued that the SEC increased investor focused oversight, monitored and mitigated COVID, and its traditional mission continued with vigor. Clayton reported that the SEC moved forward on a number of initiatives to improve proxy voting, improve access to capital, modernize the fund disclosure and regulatory framework, and improve equity market structure. Clayton addressed diversity and inclusion stating that the SEC is building a strong foundation for the OMWI office and has continued to advance initiatives on diversity and inclusion.

Member Questions

SEC Looking Forward

Chairman Crapo (R-ID) asked where the SEC and Congress should continue to focus on. Clayton answered corporate hygiene and the lesson we have all learned from a mandatory teleworking environment. He continued that more can be done to improve the electronic framework. Clayton added that the proxy process needs improvement and that companies do not have enough access to shareholder base.

Shareholder Voting

Sen. Tillis (R-NC) asked Clayton to expand on the status of the shareholder process. Clayton answered that this has not been updated since the 1950s and the SEC is on the proposal process which looked at what a meaningful stake in

a company means and the amount one would need to show commitment that allows attention. Clayton wanted to update this because resubmission thresholds are outdated.

Sen. Rounds (R-SD) wondered if there should be more disclosures for proxy advisory firms and asked for Clayton's thoughts on regulatory authority that should involve those firms. Clayton replied that the proxy process is designed to proximate shareholder meetings and would apply this concept to firms.

ESG

Chairman Crapo (R-ID) asked what else the SEC and Congress should focus on and Clayton said the SEC has taken a rigorous approach to ESG disclosure and welcomes OMB's recent report.

Sen. Warren (D-MA) accused the SEC leadership of doing nothing for climate change which has resulted in multiple problems. She asked multiple times if the SEC has uniform standards for climate risk reporting. Clayton responded no but the SEC had a materiality standard. She followed up asking if the SEC mandated publicly traded companies to report something on climate risk so investors can take that into consideration; Clayton said no. Warren questioned how Clayton can explain that investors are somehow better off with less information on climate change. Clayton answered that there is an ongoing conversation on how to address this issue in a meaningful way.

Sen. Schatz (D-HI) referenced 2010 guidance on climate risk exposure and asked for an update on enforcement efforts. Clayton responded that this is an area where certain sectors and companies all believe disclosures are required. On what the SEC has been doing, Clayton said it is determining how we drive standards meaningfully and that they need to be sector specific. He continued that it is really hard to make forward looking disclosures that would hold accurate over time and would need something to disclose against. Clayton went on that the SEC is working on that and believed that one can start to see metrics where people will gravitate toward. Schatz echoed Warren that the SEC needs a uniform platform and disclosure requirements. He questioned how deeply engaged Clayton was with international counterparts on physical risk and next steps for the SEC. Clayton replied that the SEC is engaged in a monthly, if not weekly, process. He advised to be humble about this and the need for a disclosure that is forward looking but not held to precision. Clayton thought there would be better disclosure if there was a safe harbor.

COVID-19 Response

Chairman Crapo said that tools like the market wide circuit breakers oversaw the physical floors of the stock exchanges and mentioned temporary relief in other areas. He asked about the temporary actions the SEC has taken in reaction to the pandemic and if any of those actions should become permanent. Clayton replied that the shift to mandatory teleworking environment should be permanent as it showed the importance of conducting business electronically and remotely.

Sen. Tillis (R-NC) asked what Clayton is doing in his remaining weeks as SEC Chairman. Clayton responded that he is focused on COVID and keeping an eye on the markets.

Human Capital

Chairman Crapo referred to the Uyghur Forced Labor Prevention Act (S. 3471 and H.R. 6210) which would create a new disclosure regime at the SEC to deal with human rights violations. He was concerned that this may not be the right approach and asked Clayton for his advice if the SEC needs to establish a new regime instead of focusing on our established regimes. (QFR)

Sen. Warner (D-VA) focused on human capital reporting and appreciated the SEC laying down the first step on this front. He continued that Regulation S-K, for the first time, required a level of human capital metrics and hoped to eventually collect enough data in place where there is a baseline to allow some comparison between industries on this topic. Warner noted that Clayton believes in a principals-based approach and asked him to talk about how he saw that occurring in practice and how we make sure that more firms have human capital fall into the materiality category and take it seriously. Clayton believed that the disclosure requirement put in place will facilitate qualitative disclosure and expected turnover in particular areas to be metric. He thought it was of value to understand what management believes on driving the value of business from a human capital perspective. Warner wanted to go further with this subject and hoped that Clayton is open about accounting treatment on investing and human capital.

Stock Buybacks

Ranking Member Brown (D-OH) stated that Congress is calling on the SEC to revisit the stock buyback rule and wanted clear standards instead of expanding resources on weak enforcement activities. Clayton responded that additional hygiene on 10B51 plans is appropriate. He explained that the buyback provides an efficient way to manage capital allocation and balance sheets. For executives, Clayton is a proponent of a cooling-off period - when a company puts a 10b5-1 plan in place, there are no purchases or sales, in most cases it's sales with an executive 10b5-1 program, for a period of time.

Sen. Van Hollen (D-MD) referenced the SEC rule 10B51 which allows executives an affirmative defense to insider trading if they provide a schedule for their stock sales but there have been a number of incidents that undermine public perception. Van Hollen encouraged guardrails against this and the need to act. He asked if Clayton agreed on the need for tighter guardrails to protect against potential abuse. Clayton agreed as a general matter and repeated his support for a cooling off period for executives using 10B51 plans.

IPOs

Sen. Toomey (R-PA) remarked that there are fewer companies going public and questioned if there was more that Congress could do to create an environment that is more attractive to allow companies to go public earlier. Clayton replied that the Jobs Act was a great piece of legislation providing an on ramp and expanded access for companies. He reported that IPOs are up and recognized that a one size fits all is not a good system for companies.

Technology and Innovation

Sen. Scott (R-SC) stated that technology and innovation has improved the availability of simple and low-cost platforms for investors and because of this, many more people, especially young people, are engaged in the stock market. He asked Clayton to discuss the benefits of this increase participation and if the SEC is keeping up with this. Clayton answered that being connected to our financial system is essential to participation in our society and wanted to increase those connections by preserving investor protection and driving down costs. Scott agreed that access is

so critical, and accessibility has never been more available than it is today. He felt that we are moving to a place where the average family and individual will have access to the stock market and have integrity in the system.

Sen. Menendez (D-NJ) asked if Clayton agreed that diversity on executive teams increases profitability, specifically for media and technology companies. Clayton agreed and talked about the SEC's actions around diversity and inclusion and he felt they were value enhancing which led to better performance.

Sen. Cortez Masto (D-NV) touched on investor protection for unsophisticated investors, young people trading online which, in her opinion, gamifies the stock market. She asked what the SEC has done to avoid financial devastation for investors and what it is doing about these platforms. Clayton responded that the SEC has put out guidance to tell people, investors, broker dealers, and the platforms that people trading those instruments have the capability of understanding those instruments.

Beneficial Ownership

Sen. Menendez (D-NJ) focused on foreign actors evading the beneficial ownership disclosure requirement under 13D and encouraged the SEC to continue to be vigilant against foreign actors. He asked about any improvements to 13D oversight since last year. Clayton agreed that understanding the beneficial ownership and whether there's any evasion of 13D is very important. Clayton reported that the SEC put out guidance addressing foreign omnibus accounts- accounts that mix ownership of different parties outside the U.S. and then trade through a single -pipe into the U.S. to mask ownership.

Clayton said we need to ensure that the U.S. broker dealers particularly -- and this guidance comes out in the area of thinly traded and low price securities -- are doing the appropriate diligence on those foreign omnibus accounts.

Dodd-Frank Act

Sen. Menendez (D-NJ) referenced Section 956 of Dodd Frank which requires the agencies to issue a joint purpose executive compensation rule, he questioned if all the six agencies have sat down to discuss the rule making. Clayton responded yes and the rule is in the advance term sheet stages, but the bandwidth has been constrained by COVID. Regulation Buy Enforcement

Sen. Cotton (R-AR) remarked that the enforcement decisions are often based on things investors may or may not like. He asked if Clayton agreed that enforcement actions should only be taken when an investor violates rules created by law through Congress or rules passed into regulation. Clayton agreed on that but disagreed that we should expand authority of regulation without notice and comment. Cotton moved on to the SEC share-class election disclosure initiative and questioned if the SEC can site a public document on this. Clayton did not have a document at hand but understood the issue. He explained that the share-class initiative tried to deal with what the SEC saw as an inconsistent widespread practice. Clayton hoped that there is clarity brought to this.

Accredited Investors

Sen. Rounds (R-SD) referenced SEC's expansion of people that qualify as accredited investors under Regulation D and appreciated the expansion to Native American tribes. He explained that the reforms will make it easier for tribes to participate in investment opportunities and will also put Native American tribes on more equal footing with other investors in market participants.

In considering the changes to Reg D, particularly as it relates to Native American tribes, he asked if there are additional ways the SEC and Congress can help level the regulatory playing field for tribes. Clayton responded yes and stated tribes should be treated like any other institutional investor and will be treated as such going forward.

Financial Transaction Tax

Sen. Rounds (R-SD) expressed concern with a financial transaction tax on security trading. Clayton clarified that the transaction tax falls on the investor and if there was a piece meal approach to this, there will be critical infrastructure problems which would create operational issues.

Sen. Rounds (R-SD) wondered if there should be more disclosures for proxy advisory firms and asked for Clayton's thoughts on regulatory authority that should involve those firms. Clayton replied that the proxy process is designed to approximate the quintessential shareholder meeting. He went on to say that if you have somebody at that shareholder meeting who is soliciting votes one way or another; you want to know their interest. Clayton said that what they've done in their rulemaking is to apply that concept to the proxy advisory firms and to the extent you have material, not absolute material conflicts but where a reasonable person could believe the conflict would affect your advice, you should tell them.

Form 13F

Sen. Cortez Masto (D-NV) asked if Clayton was going to finalize proposed rule 13F before he leaves his position, she thought this rule was controversial. Clayton responded no and that the proposal has taught the SEC something. He explained that 13F was being used in unintended ways like companies finding shareholders and tracking trading strategies which he said was an inefficient way of doing that. Clayton added that the SEC was not sure it wanted regulation there to facilitate but if it does, it would not be done through 13F.