Testimony on "Oversight of the U.S. Securities and Exchange Commission"
by
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Chairman Shelby, Ranking Member Brown, and Members of the Committee:

Thank you for inviting me to testify today regarding the current work and initiatives of the U.S. Securities and Exchange Commission (SEC or Commission).[1] The SEC is a critical agency that serves as the bulwark safeguarding millions of investors and the most vibrant markets in the world. Thanks to the exceptional work and commitment of our superb staff, the Commission has in recent years strengthened its operations and programs across the agency – aggressively enforcing the securities laws to punish wrongdoers, adopting strong measures that protect investors and our markets, and investing in the people and technology required to ensure that our markets remain the strongest and safest in the world. These and other efforts across our extensive areas of responsibility are all in furtherance of our essential mission: to protect investors; to maintain fair, orderly, and efficient markets; and to facilitate capital formation.

The Commission's actions and accomplishments since I testified before this Committee in September 2014 have been extensive.[2] Each of the last three years has been marked by vigorous enforcement and examination programs, empowered with new tools and methods to detect and hold wrongdoers accountable and protect investors. In fiscal year 2015 alone, the Commission brought over 800 enforcement actions, an unprecedented number; secured over $4 billion in orders directing the payment of penalties and disgorgement, an all-time high; performed approximately 2,000 exams, a five-year high; and, even more importantly, continued to develop cutting-edge cases and smarter, more efficient exams. Aided by enhanced technology to analyze suspicious activity and strengthened by initiatives like self-reporting, SEC staff has been able to identify and target the most significant risks for investors across the market.

The Commission over the last three years has pursued very consequential rulemaking and other measures designed to protect investors, strengthen the markets, and open new avenues for capital-raising. Since I last testified, the agency, for example, has advanced major rules addressing important equity market structure issues – including controls on the technology used by key market participants, the transparency of alternative trading systems, and the consolidated

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[1] The views expressed in this testimony are those of the Chair of the Securities and Exchange Commission and do not necessarily represent the views of the President, the full Commission, or any Commissioner.

[2] *See generally SEC Accomplishments: Protecting Investors and Our Markets Through Rigorous Oversight, Vigorous Enforcement, and Transformative Rulemaking* (June 13, 2016), *available at* https://www.sec.gov/about/sec-accomplishments.htm.

audit trail – while moving forward with a comprehensive assessment of other fundamental structural questions. We also issued a series of proposals to address the increasingly complex portfolios and operations of mutual funds and exchange-traded funds (ETFs). We adopted new rules for crowdfunding and smaller securities offerings under Regulation A, while proposing additional avenues for small businesses to raise capital. We finalized critical components of the regulatory regime for security-based swaps. We also proposed the full suite of rules regarding executive compensation practices. And we continued to execute a comprehensive review of the effectiveness of our disclosure regime.

This work, which is described in greater detail below, marks the latest phase of an extraordinary regulatory effort by the agency since before I became Chair, enlisting all of our policy divisions and offices. Beyond our discretionary initiatives, the Commission has now adopted final rules for 66 of the 86 mandatory rulemaking provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) directed to the SEC, the majority of them since I became Chair.[3] We have completed all of the rulemakings directed by the Jumpstart Our Business Startups Act (JOBS Act). And we have made significant progress advancing the rulemakings required of us late last year under the Fixing America's Surface Transportation Act (FAST Act). Some of the most significant initiatives of the last three years include:

- *Equity Market Structure*. An imperative of our modern equity markets is strong technological systems and operations, and the Commission has adopted Regulation Systems Compliance and Integrity (SCI) to require critical market participants – including exchanges, clearing agencies, and large alternative trading systems (ATSs) – to implement wide-ranging measures designed to reduce the occurrence of systems issues and improve resilience when such issues do occur. The self-regulatory organizations (SROs), acting under Commission oversight, have also continued to develop further measures to enhance the operational integrity of the markets. In addition, the Commission has proposed new rules to enhance market transparency, with the first-ever major update of Regulation ATS, and I expect that we will very soon propose rules requiring important new disclosures for how investor orders are handled by broker-dealers. The Commission has also proposed enhancements to our core regulatory tools of registration and firm oversight. And we have put out for notice and comment the final plan for the consolidated audit trail, as well as expanded our consideration of additional market structure reforms through the establishment of the Equity Market Structure Advisory Committee.

- *Money Market Funds and Asset Management.* To address the risk of investor runs, as experienced during the financial crisis, the Commission in 2014 adopted rules that fundamentally change the way money market funds operate, rules that will become fully operational this coming October. Following that work, the Commission undertook to enhance its regulatory regime for the broader asset management industry. In furtherance

[3] The current status of the Commission's implementation of the Dodd-Frank Act is summarized at https://www.sec.gov/spotlight/dodd-frank.shtml.

of that goal, the Commission last year proposed four major rules to address potential risks in the modern asset management industry, including rules that would improve and expand the information reported to the Commission and investors, impose new controls on how funds manage their liquidity, and enhance the regulation of funds' use of derivatives.

- *Capital Formation*. Implementing mandates from the JOBS Act, the Commission adopted rules to increase access to capital for smaller companies by revamping and enhancing Regulation A, and other rules to permit companies to offer and sell securities through equity crowdfunding. Separately, the Commission has also proposed rules to facilitate intrastate and regional securities offerings, including offerings relying upon recently adopted intrastate crowdfunding provisions under state securities laws. We also worked with the SROs to build a pilot program to widen the minimum quoting and trading increments – or tick sizes – for stocks of some smaller companies, which should aid in understanding whether wider tick sizes enhance the market quality and secondary liquidity of these stocks. This work follows on the Commission's adoption of rules to allow general solicitation for certain offers and sales made under Rule 506, as well as a rule to disqualify certain felons and other "bad actors" from participating in private securities offerings made under Rule 506.

- *Disclosure Effectiveness.* The staff of the Commission has undertaken a comprehensive assessment of the effectiveness of our disclosure regime for investors and issuers. As part of that assessment, the Commission issued a major concept release that seeks input on modernizing certain business and financial disclosure requirements in Regulation S-K for the benefit of investors and companies. We also issued a request for comment for certain financial reporting and disclosure requirements in final statements under Regulation S-X. I expect that the Commission will also shortly propose revisions to Industry Guide 7, which applies to disclosures about the projections and properties of mining companies.

- *Security-Based Swaps.* The Commission has implemented a substantial portion of a regulatory regime for security-based swaps required by the Dodd-Frank Act, which is designed to ensure that the $11 trillion market for security-based swaps is safer, more transparent, and more efficient. Since I last testified, the Commission adopted the core rules for reporting security based swap transactions to regulators and the public through security-based swap data repositories. We also adopted the framework for registering security based swap dealers and major security-based swap participants with the Commission, as well as rules to help ensure that non-U.S. dealers participating in the U.S. market comply with our rules. Most recently, the Commission adopted extensive requirements for how these entities must conduct business with counterparties and acknowledge and verify their transactions. Finalizing the remainder of the rules for trade reporting and dealers activities – and operationalizing those regimes – is a priority for 2016.

- *Asset-Backed Securities.* The Commission in 2014 adopted wide-ranging rules to enhance transparency and better protect investors in the asset-backed securities market.

The Commission completed rules requiring significant enhancements to registered offering disclosures for asset-backed securities, a market with $4.8 trillion in issuances over the past decade that stood at the epicenter of the financial crisis. Since I last testified, acting jointly with five other federal agencies, the Commission also adopted credit risk retention rules, which require securitizers of asset-backed securities to keep "skin in the game" for the securities they package and sell.

- *Executive Compensation.* In 2015, the Commission adopted the rule mandated by the Dodd-Frank Act requiring a company to disclose the ratio of compensation of its chief executive officer to the median compensation of its employees. The Commission in 2015 also proposed the remaining executive compensation rules required by the Dodd-Frank Act, including disclosure of whether a company allows executives to hedge the company's stock, disclosure of pay versus performance measures of executive compensation, and new disclosures and rules for clawing back incentive compensation erroneously awarded. We also in 2016 re-proposed, jointly with other regulators, rules regarding disclosure and restrictions for certain incentive-based compensation arrangements at large financial institutions.

- *Credit Rating Agencies and Credit Ratings.* The Commission has adopted a comprehensive package of reforms in 2014 for the regulation and oversight of credit ratings agencies, including new controls on the management of conflicts of interest. The Commission has also acted to remove almost all of the references to credit ratings from its rules and forms.

- *Broker-Dealer Financial Responsibility.* The Commission, soon after I became Chair, adopted rules to provide additional safeguards with respect to a broker-dealer's custody of customer securities and cash, as well as to strengthen the audit requirements for broker-dealers. In addition, the Commission adopted amendments to the broker-dealer financial responsibility rules to enhance protections for customer assets, firm capital requirements, and risk management controls. In 2016, we proposed, jointly with the Federal Deposit Insurance Corporation (FDIC), rules that implement procedures for the orderly liquidation of covered broker-dealers.

- *Municipal Advisors.* The Commission has established a new regulatory regime to protect municipalities and investors from conflicted advice and unregulated advisors by requiring municipal advisors to register with the SEC and to comply with the rules of the Municipal Securities Rulemaking Board (MSRB). And we continue to work with the MSRB to establish the full suite of regulatory obligations for municipal advisors.

- *Volcker Rule*. The Commission, in December 2013, adopted, jointly with other regulators, rules to implement a prohibition on proprietary trading and certain relationships with hedge funds and private equity funds. Compliance with those rules was required in 2015, and the SEC is now working in coordination with the other financial regulators to ensure that firms have taken the necessary steps.

While our work in enforcement and rulemaking are perhaps the most prominent examples of the agency's achievements, the imperatives of our mission are carried forward each day by all of the dedicated staff of our divisions and offices. The Division of Corporation Finance, for example, reviews the annual and periodic reports of thousands of issuers each year, helping to ensure that investors receive full and fair disclosure about the public companies in which they invest. And staff in the Office of Small Business Policy alone responded last year to over a thousand inquiries from small businesses about their questions and concerns. During the same period, the Division of Trading and Markets reviewed more than 2,100 filings from exchanges and other SROs to preserve a fair and orderly marketplace for all investors. The Division of Investment Management reviewed filings last year covering more than 12,500 mutual funds and other investment companies, where many individuals invest their hard-earned money to save for retirement, college, and other important goals. Our economists in the Division of Economic and Risk Analysis produced more than 30 incisive papers and publications in 2015, including two major analyses to help inform our work on asset management. And the numbers are only a small part of the story. Each instance of such engagement makes our markets better and safer for investors.

Throughout the agency, we are increasingly harnessing technology to better identify risks, uncover frauds, sift through large volumes of data, inform policymaking, and streamline operations. The Commission's emphasis on technological improvements is continuing to pay dividends, improving efficiencies while allowing us to cover more ground than ever before. We continue to build on this progress by seeking sufficient appropriated funds for a number of key information technology (IT) initiatives, including improvements to the Electronic Data Gathering, Analysis and Retrieval (EDGAR) system and our enforcement surveillance tools.

While the Commission today is stronger and more effective than ever before, challenges remain if we are to continue our current trajectory and address the growing size and complexity of the securities markets. We now oversee approximately 28,000 market participants and selectively review the disclosures and financial statements of over 9,000 reporting companies. From 2001 to 2015, assets under management of SEC-registered advisers more than tripled from approximately $21.5 trillion to approximately $66.8 trillion, and assets under management of mutual funds more than doubled from $7 trillion to over $15 trillion. Trading volume in the equity markets from 2001 through 2015 nearly tripled to over $70 trillion. And, as this Committee knows, the SEC's responsibilities have also significantly increased, with new or expanded responsibilities for security-based derivatives, hedge fund and other private fund advisers, credit rating agencies, municipal advisors, clearing agencies, and crowdfunding portals. As I have testified before both the House and Senate, the SEC is significantly under-resourced for the extensive responsibilities it has, even though our budget is deficit neutral and funded by very modest transaction fees.

It is critical that we have the resources necessary to discharge our responsibilities, both the new ones and the many others we have long held in the face of a growing and ever-more sophisticated financial services industry. I deeply appreciate the serious charge we have to be prudent stewards of the funds we are appropriated, and we strive to demonstrate how seriously we take that obligation by the work we do. At the same time, the cuts and limitation to the SEC's budget that some have proposed would imperil the progress we have made and our ability

to fulfill our mission. Only with Congress' continued assistance can we continue to successfully execute our mission to protect investors, preserve the integrity of our markets, and promote capital formation. We very much appreciate the Committee's support.

Vigorously Enforcing the Securities Laws

The SEC's vigorous enforcement program is at the heart of our efforts to protect investors and instill confidence in the integrity of the markets. The Division of Enforcement (Enforcement) advances these efforts by investigating and bringing civil charges against violators of the federal securities laws. Successful enforcement actions impose meaningful sanctions on securities law violators, result in penalties and disgorgement of ill-gotten gains that can be returned to harmed investors, and deter future wrongdoing.

Enforcement delivered very strong results on behalf of investors in FY 2014, FY 2015 and continues to do so in FY 2016. The SEC filed a record 807 enforcement actions in FY 2015 covering a wide range of misconduct, and obtained orders totaling $4.19 billion in disgorgement and penalties, both at record levels. Of the 807 enforcement actions, a record 507 were independent actions for violations of the federal securities laws, and 300 were either actions against issuers who were delinquent in making required filings with the SEC or administrative proceedings seeking bars against individuals based on criminal convictions, civil injunctions, or other orders.

Even more important than the numbers, these actions addressed many of the most important issues for investors and markets, spanned the securities industry, and included numerous "first-of-their-kind" actions. Significantly, approximately two-thirds of our substantive actions in FY 2015 also included charges against individuals. A few other important features of our enforcement program also bear highlighting.

Executing the Admissions Policy

The Commission continues to use its first of its kind admissions policy to aggressively seek admissions in certain cases where heightened accountability and acceptance of responsibility by a defendant is particularly important and in the public interest. These types of cases include those involving particularly egregious conduct; where large numbers of investors were harmed; where the markets or investors were placed at significant risk; where the conduct undermines or obstructs our investigative process; where an admission can send an important message to the markets; or where the wrongdoer presents a particular future threat to investors or the markets. Since implementing the admissions protocol in 2013, the SEC has obtained admissions from over 50 entities and individuals, including major financial institutions and national auditing firms. We also required individuals to admit wrongdoing in a number of cases, including a world-wide pyramid scheme targeting the Asian-American community.[4] While this

[4] We also do not accept "neither admit nor deny" settlements where a defendant has acknowledged relevant facts in a settlement with other criminal or civil authorities, or been convicted. This regularly occurs in connection with

is an evolving protocol that continues to be applied to more cases, as we indicated when we implemented it, the majority of cases will continue to be resolved on a "neither admit nor deny" basis, which is the norm for other civil law enforcement agencies and in private litigation.[5] We are committed, however, to requiring admissions where appropriate, and are prepared to litigate those cases if necessary.

Enhancing Focus on Key Areas of Misconduct

The Commission also continues to focus resources on key areas of misconduct. One critical area is financial reporting and issuer disclosure. Comprehensive, accurate, and reliable financial reporting is the bedrock upon which our markets are based, and is essential to ensuring public confidence in them. And at my direction, since 2013, our Enforcement Division has intensified its focus on pursuing violations in this area. Part of this effort involved creating a dedicated group of accountants, attorneys, and analysts who use cutting edge data analytical tools to look for evidence of reporting discrepancies and other early warning signs of financial reporting fraud. The SEC brought a series of significant financial reporting cases in FY 2015, including four emblematic actions last September, each of which involved sophisticated

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guilty pleas that arise from parallel criminal investigations, which frequently are matters that we referred to a criminal prosecutor in which our own investigation assisted in securing a favorable resolution on the criminal side as well. While these cases are not included in the admissions cited above, they serve the same purpose and have the same impact. We have obtained these kinds of settlements with dozens of individuals and entities since this policy changed at the end of 2011.

[5] In the majority of its cases, the Commission, like all other federal agencies with civil law enforcement powers, determines that it is appropriate to continue to settle on a "no admit, no deny" basis. This practice allows the Commission to obtain significant relief, eliminate litigation risk, return money to victims more expeditiously, and conserve enforcement resources for other matters. But, in 2013, we determined that our Enforcement program's deterrent message could be enhanced by requiring admissions of wrongdoing in appropriate cases. We are pleased to see that other civil law enforcement agencies have begun to follow our lead. For example, the CFTC requires admissions in certain cases and entered into its first admissions settlement in October 2013. *See* Release PR6737-13, *CFTC Files and Settles Charges Against JPMorgan Chase Bank, N.A., for Violating Prohibition on Manipulative Conduct In Connection with "London Whale" Swaps Trades*, Oct. 16, 2013, http://www.cftc.gov/PressRoom/PressReleases/pr6737-13 [Max Stendahl, *CFTC Mimics SEC Policy Shift With JPMorgan 'Whale' Pact*, Law360 (Oct. 16, 2013, 7:47 p.m.), http://www.law360.com/articles/480686/cftc-mimics-sec-policy-shift-with-jpmorgan-whale-pact]. Similarly, the CFPB requires admissions in certain cases and entered into its first admissions settlement in February 2014. *See* Press Release, *CFPB Takes Action Against Mortgage Lender for Illegal Payments*, Feb. 24, 2014, http://www.consumerfinance.gov/about-us/newsroom/cfpb-takes-action-against-mortgage-lender-for-illegal-payments/.

disclosure violations or cleverly masked reporting fraud.[6] Each of these cases also involved charges against senior executives. Holding individuals accountable for their role in financial misconduct is a significant priority of mine and in FY 2015, we charged 120 individuals in our substantive issuer reporting and disclosure cases, approximately twice the number of individuals we charged in FY 2014.

Another key area of enforcement is investment management, where the SEC has continued to bring actions addressing a widening range of issues, including performance advertising, undisclosed conflicts of interest, compliance issues, and private equity fees and expenses. Among these are "first-of-their-kind" actions for failures to report material compliance matters to fund boards and the improper allocation of expenses by private equity advisers. The Enforcement Division's focus on private equity has expanded significantly over the past few years and, to date, the SEC has brought eight enforcement actions related to private equity advisers breaching their fiduciary duties by charging undisclosed fees and expenses, shifting and misallocating expenses, and failing to adequately disclose conflicts of interest.

In addition, since I last testified before the Committee, Enforcement has emphasized market structure issues, bringing significant enforcement actions involving high frequency trading, the operation of trading platforms such as dark pools, manipulative trading, and market access and technology controls. We have brought cases, for example, against ATSs for misusing confidential customer trading information, actions against high frequency traders for manipulative trading and net capital violations, and against exchanges for providing some, but not all, traders with additional information about certain order types.

Enhancing the Whistleblower Program

The SEC's Whistleblower program continues to have a transformative impact on our enforcement program. The SEC's Office of the Whistleblower is currently tracking hundreds of matters in which a whistleblower's tip has caused a matter under investigation or an investigation to be opened, or which have been forwarded to Enforcement staff for consideration in connection with an existing investigation. The number of whistleblower tips received by the Commission has increased each year of the program's operation. In Fiscal Year 2015, the Commission received nearly 4,000 whistleblower tips, representing a 30% increase over the number of tips received in Fiscal Year 2012, the first year for which the office had full-year data. In FY 2015, the Commission paid more than $37 million to whistleblowers who provided original information that led to successful enforcement actions resulting in an order or monetary

[6] *See* Press Release No. 2015-184, *SEC Charges BDO and Five Partners in Connection With False and Misleading Audit Opinions* (Sept. 9, 2015), *available at* https://www.sec.gov/news/pressrelease/2015-184.html; Press Release No. 2015-179, *SEC Charges Sports Nutrition Company With Failing to Properly Disclose Perks for Executives* (Sept. 8, 2015) available at https://www.sec.gov/news/pressrelease/2015-179.html; Press Release No. 2015-180, *SEC Charges Bankrate and Former Executives With Accounting Fraud* (Sept. 8, 2015), available at https://www.sec.gov/news/pressrelease/2015-180.html; and Press Release No. 2015-183, *SEC Charges Video Management Company Executives With Accounting Fraud* (September 8, 2015), available at https://www.sec.gov/news/pressrelease/2015-183.html.

sanctions exceeding $1 million, and has awarded more than $50 million since the program's inception. Just last week, the Commission announced a $17 million award, its second largest, to a former company employee whose detailed tip substantially advanced Enforcement's investigation. The Commission has also filed numerous "friend of the court" briefs in support of private actions by whistleblowers who have experienced retaliation for reporting internally at their companies, and has brought our own actions against firms for whistleblower retaliation and improper restrictions of whistleblowing activity in confidentiality agreements.

Preserving Investigative Tools

During my tenure as Chair, I have sought to work with Congress to modernize the Electronic Communications Privacy Act (ECPA), which governs the authority of law enforcement to obtain emails from internet service providers (ISPs). The bills currently pending in Congress to amend ECPA would unfortunately pose significant risks to the American investing public by impeding the ability of Commission staff to investigate and uncover insider trading, Ponzi schemes, and other types of fraud. Although I agree that ECPA's privacy protections and evidence collection procedures should be updated, I believe there are ways to update ECPA that offer stronger privacy protections and observe constitutional boundaries without putting innocent victims and our capital markets at risk.

As drafted, the bills would require government entities to obtain a criminal warrant when they seek the content of subscriber emails and other electronic communications from ISPs. The SEC, as a civil law enforcement agency, cannot obtain criminal warrants. Thus, the SEC would no longer be able to gather these communications directly from an ISP to obtain often critical and otherwise unobtainable evidence of serious wrongdoing. Any effort to update ECPA can, and should, be done without harming the ability of the SEC to protect our nation's citizens from securities fraud. I look forward to the opportunity to continue to work with Congress on solutions that both protect investors and privacy interests.

Building Stronger, Safer Markets for Investors and Issuers

The SEC continues to pursue an extensive program of rulemaking and other policy efforts designed to ensure that our securities markets continue to optimally and securely serve investors and issuers. Since I last testified before the Committee, the SEC has significantly progressed in implementing mandatory rulemakings under three separate statutes, as well as in pursuing an impressive range of important discretionary initiatives.

As the Committee knows, the SEC and our fellow regulators have been working hard to strengthen our nation's financial systems by implementing the rules mandated by the Dodd-Frank Act, which responded to the worst financial crisis since the Great Depression. Over the last two years, the SEC has moved into the final phase of implementing the Dodd-Frank Act, focusing on completing all of the remaining rules in the two major remaining areas of mandates: security-based swaps and executive compensation.

Increasing Transparency and Oversight for Security-Based Swaps

Since September 2014, we have marked several milestones in the establishment of a comprehensive regulatory framework for security-based swaps, which will give us powerful tools to oversee an $11 trillion market. First, we finalized the core requirements for reporting security-based swap transactions to regulators and the public through security-based swap data repositories,[7] and we proposed additional requirements to ensure that reporting will produce accurate data for regulators and market participants.[8] With the adoption of these rules expected later this year, the regulatory infrastructure for transaction reporting will be complete.

Second, we adopted the framework for registering security-based swap dealers and major security-based swap participants with the Commission,[9] as well as rules to help ensure that non-U.S. dealers participating in the U.S. market comply with our rules.[10] Work is now underway to finalize the obligations that registered dealers and participants will be required to undertake. In April, the SEC adopted extensive requirements for how these entities must conduct business with counterparties – including special entities like municipalities and pension funds – and supervise such conduct.[11] We also this month finalized rules for timely and accurate trade acknowledgment and verification requirements for security-based swaps,[12] and have proposed a

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[7] *See* Release No. 34-74246, *Security-Based Swap Data Repository Registration, Duties, and Core Principles* (February 11, 2015), *available at* https://www.sec.gov/rules/final/2015/34-74244.pdf.; Release No. 34-74244, *Regulation SBSR—Reporting and Dissemination of Security-Based Swap Information* (February 11, 2015), *available at* https://www.sec.gov/rules/final/2015/34-74244.pdf.

[8] See Release No. 34-74245, *Regulation SBSR – Reporting and Dissemination of Security-Based Swap Information* (February 11, 2015), *available at* https://www.sec.gov/rules/proposed/2015/34-74245.pdf; Release No. 34-76624, *Establishing the Form and Manner with which Security-Based Swap Data Repositories Must Make Security-Based Swap Data Available to the Commission*,(December 11, 2015), *available at* https://www.sec.gov/rules/proposed/2015/34-76624.pdf; and Release No. 34-75845, *Access to Data Obtained by Security-Based Swap Data Repositories and Exemption from Indemnification Requirement* (September 4, 2015), *available at* https://www.sec.gov/rules/proposed/2015/34-75845.pdf.

[9] *See* Release No. 34-75611, *Registration Process for Security-Based Swap Dealers and Major Security-Based Swap Participants* (August 5, 2015), *available at* https://www.sec.gov/rules/final/2015/34-75611.pdf.

[10] *See* Release No. 34-77104, Security-Based Swap Transactions Connected with a Non-U.S. Person's Dealing Activity That Are Arranged, Negotiated, or Executed By Personnel Located in a U.S. Branch or Office or in a U.S. Branch or Office of an Agent; Security-Based Swap Dealer De Minimis Exception (Feb. 10, 2016), *available at* https://www.sec.gov/rules/final/2016/34-77104.pdf; and Release No. 34-72472, *Application of "Security-Based Swap Dealer" and "Major Security-Based Swap Participant" Definitions to Cross-Border Security-Based Swap Activities* (June 25, 2014), *available at* https://www.sec.gov/rules/final/2014/34-72472.pdf.

[11] *See* Release No. 34-77617, *Business Conduct Standards for Security-Based Swap Dealers and Major SecurityBased Swap Participants (April 14, 2016), available at* https://www.sec.gov/rules/final/2016/34-77617.pdf.

[12] *See* Release No. 34-78011, *Trade Acknowledgment and Verification of Security-Based Swap Transactions* (June 8, 2016), *available at* https://www.sec.gov/rules/final/2016/34-78011.pdf.

process for dealing with bad actors in the security-based swap market.[13] Next in line will be to finalize that process, complete capital, margin, and asset segregation requirements for security-based swap entities,[14] and adopt rules for recordkeeping and regulatory reporting.[15] With those steps, the regulatory structure for security-based swap dealers will be complete, a priority supported by all of the Commissioners.[16] Our goal is to finalize those rules by year-end.

Creating New Disclosures and Limits for Executive Compensation

With respect to executive compensation, the SEC last year issued proposals for all of the remaining executive compensation rulemakings required by the Dodd-Frank Act, including disclosure of whether a company allows executives to hedge the company's stock, disclosure of pay versus performance measures of executive compensation, and new disclosures and rules for clawing back incentive compensation erroneously awarded.[17] Together with five of our fellow financial regulators, we also re-proposed a joint rule regarding incentive-based compensation arrangements at large financial institutions.[18] The final rules are expected to be advanced expeditiously. And following the analysis of some 285,500 total comment letters, 1,500 of them unique, the final pay ratio rule was adopted in August 2015.[19]

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[13] *See* Release No. 34-75612, *Applications by Security-Based Swap Dealers or Major Security-Based Swap Participants for Statutorily Disqualified Associated Persons to Effect or Be Involved in Effecting Security-Based Swaps* (August 5, 2015), *available at* https://www.sec.gov/rules/proposed/2015/34-75612.pdf.

[14] *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), *available at* https://www.sec.gov/rules/proposed/2012/34-68071.pdf.

[15] *See* Release No. 34-71958, *Recordkeeping and Reporting Requirements for Security-Based Swap Dealers, Major Security-Based Swap Participants, and Broker-Dealers; Capital Rule for Certain Security-Based Swap Dealers* (April 17, 2014), *available at* https://www.sec.gov/rules/proposed/2014/34-71958.pdf.

[16] *See* Commissioner Daniel M. Gallagher and Commissioner Michael S. Piwowar, *Statement Regarding Security-Based Swap Rules* (Sept. 25, 2015), *available at* https://www.sec.gov/news/statement/gallagher-piwowar-security-based-swaps.html; and Commissioner Kara M. Stein, *Remarks at the "SEC Speaks" Conference* (February 19, 2016), *available at* https://www.sec.gov/news/speech/stein-sec-speaks-2016.html.

[17] *See* Release No. 33-9723, *Disclosure of Hedging by Employees, Officers and Directors* (February 9, 2015), *available at* https://www.sec.gov/rules/proposed/2015/33-9723.pdf; Release No. 34-74835, *Pay Versus Performance* (April 29, 2015), *available at* https://www.sec.gov/rules/proposed/2015/34-74835.pdf; and Release No. 33-9861, *Listing Standards for Recovery of Erroneously Awarded Compensation* (July 1, 2015), *available at* https://www.sec.gov/rules/proposed/2015/33-9861.pdf.

[18] *See* Release No. 34-77776, *Incentive-based Compensation Arrangements* (May 6, 2016), *available at* https://www.sec.gov/rules/proposed/2016/34-77776.pdf.

[19] *See* Release No. 33-9877, *Pay Ratio Disclosure* (August 5, 2015), *available at* https://www.sec.gov/rules/final/2015/33-9877.pdf.

Completing Implementation of the Dodd-Frank Act

Beyond these two areas, the SEC has continued to finish all of the mandates of the Dodd-Frank Act since I last testified. As required by Section 1504, we re-proposed rules that would require resource extraction issuers to disclose payments made to the U.S. federal government or foreign governments for the commercial development of oil, natural gas, or minerals.[20] And, working with our colleagues at the FDIC, we proposed joint rules for broker-dealers covered under the orderly liquidation provisions of Title II, as required by Section 205(h) of the Dodd-Frank Act.[21]

These accomplishments of the last two years were, of course, only the latest in an historic undertaking by the agency to execute the most daunting rulemaking agenda in memory. Pursuant to mandates of the Dodd-Frank Act, since I arrived at the agency in April 2013, we have stood up an entirely new regulatory regime for municipal advisors,[22] and implemented sweeping changes in the securitization markets that were at the epicenter of the crisis – including the joint rulemaking on credit risk retention since I last testified before the Committee.[23] We significantly enhanced the rules for credit rating agencies,[24] strengthened the rules for how broker-dealers handle customer funds and securities,[25] disqualified bad actors from private offerings,[26] removed credit rating references from throughout our rules,[27] and, through the Volcker Rule, restricted proprietary trading by financial institutions.[28]

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[20] *See* Release No. 34-76620, *Disclosure of Payments by Resource Extraction Issuers* (December 11, 2015), *available at* https://www.sec.gov/rules/proposed/2015/34-76620.pdf.

[21] *See* Release No. 34-77157, *Covered Broker-Dealer Provisions under Title II of the Dodd-Frank Wall Street Reform and Consumer Protection Act* (February 17, 2016), *available at* https://www.sec.gov/rules/proposed/2016/34-77157.pdf.

[22] *See* Release No. 34-70462, *Registration of Municipal Advisors* (September 30, 2013), *available at* https://www.sec.gov/rules/final/2013/34-70462.pdf.

[23] *See* Release No. 34-73407, *Credit Risk Retention* (October 22, 2014), *available at* https://www.sec.gov/rules/final/2014/34-73407.pdf; and Release No. 33-9638, *Asset-Backed Securities Disclosure and Registration* (September 4, 2014), *available at* https://www.sec.gov/rules/final/2014/33-9638.pdf.

[24] *See* Release No. 34-72936, *Nationally Recognized Statistical Rating Organizations* (August 27, 2014), *available at* https://www.sec.gov/rules/final/2014/34-72936.pdf.

[25] *See* Release No. 34-70073, *Broker-Dealer Reports* (July 30, 2013), *available at* https://www.sec.gov/rules/final/2013/34-70073.pdf. In addition, the Commission adopted amendments to the broker-dealer financial responsibility rules to enhance protections for customer assets, firm capital requirements, and risk management controls and proposed rules to provide investors with useful information about modern broker-dealer order handling practices. *See* Release No. 34-70072, *Financial Responsibility Rules for Broker-Dealers* (July 30, 2013), *available at* https://www.sec.gov/rules/final/2013/34-70072.pdf.

[26] *See* Release No. 33-9414, *Disqualification of Felons and Other "Bad Actors" from Rule 506 Offerings* (July 10, 2013), *available at* https://www.sec.gov/rules/final/2013/33-9414.pdf ("Bad Actor Rule").

[27] *See* Release No. IC-31828, *Removal of Certain References to Credit Ratings and Amendment to the Issuer Diversification Requirement in the Money Market Fund Rule* (September 16, 2015), *available at* https://www.sec.gov/rules/final/2015/ic-31828.pdf; Release No. IC-30847, *Removal of Certain References to Credit*

Facilitating Capital Formation for both Large and Small Issuers

The SEC performs a critical function for issuers seeking to raise capital to grow their businesses and the larger economy. Our rules must facilitate offerings by a diverse set of companies – large and small, engaged in all manner of commerce – while ensuring that investors have the protections they require to maintain confidence in the strongest capital markets in the world. Since I last testified before this Committee, the SEC has concentrated our commitment to this responsibility through a number of key initiatives, with particular emphasis on smaller businesses.

Completing Implementation of the JOBS Act and the FAST Act

The JOBS Act, in particular, made several significant changes to the avenues for capital formation in the securities markets, especially for smaller issuers, and we have now completed all of the rules mandated by that legislation. A few months after I became Chair, we finalized the changes to private offerings required by the JOBS Act, while advancing measures to ensure the agency has the information it needs to monitor the changes and protect investors.[29] Last year, the SEC adopted final rules to update and expand Regulation A (commonly referred to as Regulation A+), an exemption from registration for small offerings of securities, to facilitate smaller companies' access to capital.[30] And we also finalized new rules to permit securities-based crowdfunding offerings by issuers and the operation of funding portals to intermediate such offerings.[31] Issuers are now actively using both of these new avenues for raising capital.

Ratings Under the Investment Company Act (December 27, 2013), *available at* https://www.sec.gov/rules/final/2013/33-9506.pdf; and Release No. 34-71194, *Removal of Certain References to Credit Ratings Under the Securities Exchange Act of 1934* (December 27, 2013), *available at* https://www.sec.gov/rules/final/2013/34-71194.pdf.

[28] *See* Release No. BHCA-1, *Prohibitions and Restrictions on Proprietary Trading and Certain Interests In, and Relationships With, Hedge Funds and Private Equity Funds* (December 10, 2013), *available at* https://www.sec.gov/rules/final/2013/bhca-1.pdf; and Release No. BHCA-2, *Treatment of Certain Collateralized Debt Obligations Backed Primarily by Trust Preferred Securities with Regard to Prohibitions and Restrictions on Certain Interests in, and Relationships with, Hedge Funds and Private Equity Funds* (January 17, 2014), *available at* https://www.sec.gov/rules/interim/2014/bhca-2.pdf.

[29] *See* Release No. 33-9415, *Eliminating the Prohibition Against General Solicitation and General Advertising in Rule 506 and Rule 144A Offerings* (July 10, 2013), *available at* https://www.sec.gov/rules/final/2013/33-9415.pdf; and Release No. 33-9416, Amendments to Regulation D, Form D and Rule 156 under the Securities Act (July 10, 2013), *available at* https://www.sec.gov/rules/proposed/2013/33-9416.pdf. On the same day, the Commission adopted rules to disqualify certain felons and other "bad actors" from participating in securities offerings made under Rule 506. *See* Bad Actor Rule, *supra* note 26.

[30] *See* Release No. 33-9741, *Amendments for Small and Additional Issues Exemptions under the Securities Act (Regulation A)* (March 25, 2015), *available at* https://www.sec.gov/rules/final/2015/33-9741.pdf.

[31] *See* Release Nos. 33-9974; 34-76324, *Crowdfunding* (October 30, 2015), *available at* https://www.sec.gov/rules/final/2015/33-9974.pdf.

The FAST Act was enacted by Congress late last year, requiring the SEC to undertake several more rules and studies to promote capital formation and modernize disclosure. We have already made progress on implementing those mandates, adopting interim final rules to revise registration forms for emerging growth companies and smaller reporting companies,[32] and to permit issuers to include a summary in the annual report on Form 10-K.[33] Earlier this year, the SEC also approved amendments to revise the rules related to the thresholds for registration, termination of registration, and suspension of reporting under Section 12(g) of the Securities Exchange Act, implementing provisions of both the JOBS and the FAST Acts.[34]

Creating New Opportunities for Smaller Issuers

The Commission has gone beyond the statutory mandates since I last testified and also developed and adopted a number of additional initiatives that are designed to facilitate capital formation, particularly for small businesses. In October 2015, for example, the Commission issued a rule proposal seeking to modernize Rule 147, a safe harbor to a statutory exemption for intrastate securities offerings, which would establish a new exemption to facilitate capital formation through intrastate offerings.[35] Many market participants and state regulators had raised concerns that the current requirements have not kept up with changes in the business environment and technology, which limits the usefulness of the safe harbor for capital-raising, especially for smaller state and local businesses. The rule proposal would retain the key feature of existing Rule 147 – its intrastate character, which permits companies to raise money from investors within their state without concurrently registering the offers and sales at the federal level. In recognition of the transformative nature of the internet and other technologies, however, the rule would, among other things, remove the existing intrastate restriction on offers, but – critically for the state-based nature of the offering and its regulation – would continue to require that sales be made only to residents of the state or territory of the issuer's principal place of business. The proposal would also modify and modernize some of the issuer eligibility requirements to make the rule available to a greater number of businesses seeking financing in-

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[32] *See* Release No. 33-10003, *Simplification of Disclosure Requirements for Emerging Growth Companies and Forward Incorporation by Reference on Form S-1 for Smaller Reporting Companies* (January 13, 2016), *available at* https://www.sec.gov/rules/interim/2016/33-10003.pdf.

[33] *See* Release No. 34-77969, *Form 10-K Summary* (June 1, 2016), *available at* https://www.sec.gov/rules/interim/2016/34-77969.pdf.

[34] *See* Release No. 33-10075, *Changes to Exchange Act Registration Requirements to Implement Title V and Title VI of the JOBS Act* (May 3, 2016), *available at* https://www.sec.gov/rules/final/2016/33-10075.pdf.

[35] *See* Release No. 33-9973, *Exemptions to Facilitate Intrastate and Regional Securities Offerings* (October 30, 2015), *available at* https://www.sec.gov/rules/proposed/2015/33-9973.pdf.

state, while requiring that such financing occur with a set of certain investor protections and that issuers have a sufficient in-state presence within the state of offering.[36]

Another important initiative is the pilot program to widen the minimum quoting and trading increments – or tick sizes – for stocks of some smaller companies. Following a study directed by the JOBS Act,[37] the Commission in May 2015 approved a proposal, submitted in response to a Commission order,[38] by the national securities exchanges and the Financial Industry Regulatory Authority (FINRA) for a two-year pilot program.[39] The SEC plans to use the pilot program to assess whether wider tick sizes enhance the market quality of these stocks for the benefit of issuers and investors. The pilot is scheduled to begin on October 3, 2016.[40]

More broadly, the Commission staff remains committed to helping small issuers use these channels and others to build their businesses using the securities markets. The Office of Small Business Policy within the Division of Corporation Finance provides extensive guidance to small businesses seeking to raise capital or comply with our reporting requirements. Each year, the office responds to over 1,000 requests for interpretive advice, provides guidance through speaking engagements, and meets frequently with interested parties about pending rulemakings that could impact small businesses. The Commission also renewed the Advisory Committee on Small and Emerging Companies to provide the Commission with advice on capital formation and reporting requirements for smaller issuers.[41]

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[36] While the proposed rule could be used for any intrastate offering meeting its conditions, more than 25 states have enacted some form of intrastate crowdfunding, and this provision could facilitate capital raising through those state provisions.

[37] *Report to Congress on Decimalization* (July 2012), *available at* https://www.sec.gov/news/studies/2012/decimalization-072012.pdf.

[38] See Release No. 34- 72460, *Order Directing the Exchanges and the Financial Industry Regulatory Authority To Submit a Tick Size Pilot Plan* (June 24, 2014), *available at* https://www.sec.gov/rules/other/2014/34-72460.pdf.

[39] *See* Release No. 34-74892, *Joint Industry Plans; Order Approving the National Market System Plan to Implement a Tick Size Pilot Program by BATS Exchange, Inc., BATS Y-Exchange, Inc., 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, New York Stock Exchange LLC, NYSE MKT LLC, and NYSE Arca, Inc., as Modified by the Commission, For a Two-Year Period* (May 6, 2015), *available at* https://www.sec.gov/rules/sro/nms/2015/34-74892.pdf.

[40] On November 6, 2015, the Commission issued an exemption to the Participants requiring implementation of the Tick Size Pilot until October 3, 2016. *See* Release No. 34-76382, Order Granting Exemption from Compliance with the National Market System Plan to Implement a Tick Size Pilot Program (November 6, 2015), *available at* https://www.sec.gov/rules/exorders/2015/34-76382.pdf.

[41] Information regarding the committee and its recommendations can be found at https://www.sec.gov/info/smallbus/acsec.shtml.

Updating the Definition of an "Accredited Investor"

In another important step for modernizing the private offering market, the Commission published a staff report in December 2015 regarding the key definition of "accredited investor," which analyzes various approaches for modifying the definition and provides staff recommendations for potential updates and modifications.[42] The report recommends that the Commission consider expanding the definition to include alternative indicators for individuals to qualify as accredited investors (other than looking solely at income and net worth). The report also evaluates the impact that potential changes to the definition would have on the size of the accredited investor pool. I have directed the staff to prepare recommendations for the Commission on how the definition should be modified, and the comments we are receiving in response to the report will help inform the next steps.

Strengthening Markets with Targeted Action and Data-Driven Analysis

Since I last testified before this Committee, we have proceeded with our ongoing assessment of U.S. equity market structure to ensure that our markets remain the deepest, fairest, and most reliable in the world. It is important that our market structure is optimally serving investors and companies of all sizes seeking to raise capital. Our approach is data-driven and includes a number of identified short-term enhancements, as well as a comprehensive review of the entire structural operation of the equity markets to determine whether other changes should be made to optimize our markets for investors and issuers. The Commission staff has also continued to pursue efforts with FINRA and the MSRB to enhance the structure of the fixed income markets.

Preserving Operational Integrity in the Equity Markets

As I have remarked since my earliest days at the Commission,[43] a fundamental requirement of our modern equity markets is strong technological systems and operations. Shortly after my appearance at the September 2014 hearing of the Committee, the Commission adopted wide-ranging rules designed to strengthen the technology infrastructure of the U.S. securities markets.[44] The rules – together comprising Regulation SCI – impose requirements on

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[42] *See Report on the Review of the Definition of "Accredited Investor"* (December 18, 2015), *available at* https://www.sec.gov/corpfin/reportspubs/special-studies/review-definition-of-accredited-investor-12-18-2015.pdf.

[43] *See, e.g.*, Chair Mary Jo White, *Enhancing Our Equity Market Structure* (June 5, 2014) *available at* https://www.sec.gov/News/Speech/Detail/Speech/1370542004312 ("Chair White Market Structure Framework Speech"); Chair Mary Jo White, *Focusing on Fundamentals: The Path to Address Equity Market Structure*, (October 2, 2013), *available at* https://www.sec.gov/News/Speech/Detail/Speech/1370539857459; and Chair Mary Jo White, Statement on Meeting with Leaders of Exchanges (September 12, 2013), available at https://www.sec.gov/News/PressRelease/Detail/PressRelease/1370539804861 ("Chair White Exchange Meeting Statement").

[44] *See* Release No. 34-73639, *Regulation Systems Compliance and Integrity* (November 19, 2014) ("Regulation SCI Adopting Release"), *available at* https://www.sec.gov/rules/final/2014/34-73639.pdf.

certain key market participants intended to reduce the occurrence of systems issues and improve resiliency when systems problems do occur.

Our efforts to preserve the operational integrity of the market extend well beyond Commission rulemaking. In response to my requests,[45] the SROs have continued to work to address issues like order types and operations, data feed disclosures, and "single points of failure" within infrastructure systems that have the ability to significantly disrupt trading.[46] Most recently, the Commission approved new rules of the New York Stock Exchange, NYSE MKT, and Nasdaq that provide for closing contingency procedures for listed securities if the relevant exchange is unable to conduct a closing transaction in one or more securities due to a systems or technical issue.[47] All of the exchanges have now conducted and completed in-depth analyses of order types and have filed proposed rule changes to clarify the operation of their order types.[48] All of the exchanges have also now submitted rule filings disclosing how they use securities information processor (SIP) feeds and direct feeds.[49] These filings provide significantly

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[45] *See, e.g.*, Chair White Market Structure Framework Speech and Chair White Exchange Meeting Statement, supra note 43.

[46] *See* Chair Mary Jo White, *The Continuous Process of Optimizing the Equity Markets* (June 2, 2016), *available a*t https://www.sec.gov/news/speech/the-continuous-process-of-optimizing-the-equity-markets.html.

[47] S*ee Release No. 34-78015, Notice of Filings of Amendment No. 1, and Order Granting Accelerated Approval of Proposed Rule Changes, as Modified by Amendment No. 1, to Provide for How the Exchanges Would Determine an Official Closing Price if the Exchanges are Unable to Conduct a Closing Transaction* (June 8, 2016), *available at* http://www.sec.gov/rules/sro/nyse/2016/34-78015.pdf ; Release No. 34-78014, *Notice of Filing of Amendment No. 1, and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment No. 1, to Establish Secondary Contingency Procedures for the Exchange's Closing Cross* (June 8, 2016), *available at* http://www.sec.gov/rules/sro/nasdaq/2016/34-78014.pdf.

[48] See Release Nos. 34-74796 (April 23, 2015), 80 Fed. Reg. 23,838 (April 29, 2015) (SR-NYSEArca-2015-08); 34-74738 (April 16, 2015), 80 Fed. Reg. 22,600 (April 22, 2015) (SR-BATS-2015-09); 34-74739 (April 16, 2015), 80 Fed. Reg. 22,567 (April 22, 2015) (SR-BYX-2015-07); 34-74558 (March 20, 2015), 80 Fed. Reg. 16,050 (March 26, 2015) (SR-NASDAQ-2015-024); 34-74618 (March 31, 2015), 80 Fed. Reg. 18,452 (April 6, 2015) (SR-Phlx-2015-29); 34-74617 (March 31, 2015), 80 Fed. Reg. 18,473 (April 6, 2015) (SR-BX-2015-015); 34-74439 (March 4, 2015), 80 Fed. Reg. 12,666 (March 10, 2015) (SR-EDGX-2015-08); 34-74435 (March 4, 2015), 80 Fed. Reg. 12,655 (March 10, 2015) (SR-EDGA-2015-10); 34-73468 (October 29, 2014), 79 Fed. Reg. 65,450 (November 4, 2014) (SR-EDGX-2014-18); 34-73592 (November 13, 2014), 79 Fed. Reg. 68937 (November 19, 2014) (SR-EDGA-2014-20); 34-73572 (November 10, 2014), 79 Fed. Reg. 68,736 (November 18, 2014) (SR-CHX-2014-18); 34-74678 (April 8, 2015), 80 Fed. Reg. 20,053 (April 14, 2015) (SR-NYSE-2015-15); and 34-74682 (April 8, 2015), 80 Fed. Reg. 20,043 (April 14, 2015) (SR-NYSEMKT-2015-22).

[49] *See* Release Nos. 34-72685 (July 28, 2014), 79 Fed. Reg. 44,889 (August 1, 2014) (SR-BATS-2014-029); 34-72687 (July 28, 2014), 79 Fed. Reg. 44926 (August 1, 2014) (SR-BYX-2014-012); 34-72682 (July 28, 2014), 79 Fed. Reg. 44,938 (August 1, 2014) (SR-EDGA-2014-17); 34-72683 (July 28, 2014), 79 Fed. Reg. 44,950 (August 1, 2014) (SR-EDGX-2014-20); 34-72711 (July 29, 2014), 79 Fed. Reg. 45,570 (August 5, 2014) (SR-CHX-2014-10); 34-72710 (July 29, 2014), 79 Fed. Reg. 45,511 (August 5, 2014) (SR-NYSE-2014-38); 34-72708 (July 29, 2014), 79 Fed. Reg. 45,572 (August 5, 2014) (SR-NYSEArca-2014-82); 34-72709 (July 29, 2014), 79 Fed. Reg. 45,513 (August 5, 2014) (SR-NYSEMKT-2014-62); 34-72684 (July 28, 2014), 79 Fed. Reg. 44956 (August 1, 2014) (SR-NASDAQ-2014-072); 34-72713 (July 29, 2014), 79 Fed. Reg. 45,544 (August 5, 2014) (SR-Phlx-2014-49); 34-72712 (July 29, 2014), 79 Fed. Reg. 45,521 (August 5, 2014) (SR-BX-2014-037); 34-74074 (January 15, 2015), 80 Fed. Reg. 3,679 (January 23, 2015) (SR-BATS-2015-04); 34-74075 (January 15, 2014), 80 Fed. Reg. 3,693 (January 23, 2015) (SR-BYX-2015-03); 34-74076 (January 15, 2014), 80 Fed. Reg. 3,674 (January 23, 2015) (SR-

improved transparency for investors and the public on how the exchanges operate. And, also at my request, the SIPs have implemented a time stamp in their data feeds, to facilitate greater transparency on the issue of data latency.[50] In this regard, it should also be noted that the SIPs have steadily upgraded their systems to reduce average latencies from nearly one second a decade ago to less than 1/1000th of a second today.[51]

Another important component of this effort is ensuring that the moderators put in place in 2012 to address extraordinary volatility in the market work well. And the SEC and the SROs are actively reviewing the operation of the limit up-limit down pilot plan, with a focus on issues that occurred during the volatile trading of August 24, 2015.[52] This review has included extensive public analysis by SEC staff of that day's events and the consideration of specific improvements to refine the plan's operation.[53]

EDGA-2015-02); 34-74072 (January 15, 2015), 80 Fed. Reg. 3,282 (January 22, 2015) (SR-EDGX-2015-02); 34-74357 (February 24, 2015), 80 Fed. Reg. 11252 (March 2, 2015) (SR-CHX-2015-01); 34-74410 (March 2, 2015), 80 Fed. Reg. 12,240 (March 6, 2015) (SR-NYSE-2015-09); 34-74409 (March 2, 2015), 80 Fed. Reg. 12,221 (March 6, 2015) (SR-NYSEArca-2015-11); 74408 (March 2, 2015), 80 Fed. Reg. 12,225 (March 6, 2015) (SR-NYSEMKT-2015-11); and 34-74690 (April 9, 2015), 80 Fed. Reg. 20282 (April 15, 2015) (SR-NASDAQ-2015-033).

[50] *See* Release No. 34-75505, *Joint Industry Plan; Order Approving Amendment No. 35 to the Joint Self-Regulatory Organization Plan Governing the Collection, Consolidation and Dissemination of Quotation and Transaction Information for Nasdaq-Listed Securities Traded on Exchanges on an Unlisted Trading Privileges Basis Submitted by the 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., International Securities Exchange LLC, NASDAQ OMX BX, Inc., NASDAQ OMX PHLX LLC, Nasdaq Stock Market LLC, National Stock Exchange, Inc., New York Stock Exchange LLC, NYSE MKT LLC, and NYSE Arca, Inc.* (July 22, 2015), *available at* https://www.sec.gov/rules/sro/nms/2015/34-75505.pdf; and Release No. 34-75505, Order Approving the Twenty Second Substantive Amendment to the Second Restatement of the CTA Plan and Sixteenth Substantive Amendment to the Restated CQ Plan (July 22, 2015), *available at* https://www.sec.gov/rules/sro/nms/2015/34-75504.pdf.

[51] *See, e.g.*, Release No. 34-70010, Notice of Filing and Immediate Effectiveness of the Nineteenth Charges Amendment to the Second Restatement of the CTA Plan and Eleventh Charges Amendment to the Restated CQ Plan (July 19, 2013), *available at* https://www.sec.gov/rules/sro/nms/nmsarchive/nms2013.shtml.

[52] *See* Release No. 34-77679, Order Approving the Tenth Amendment to the National Market System Plan to Address Extraordinary Market Volatility by Bats BZX Exchange, Inc., Bats BYX Exchange, Inc., Chicago Stock Exchange, Inc., Bats EDGA Exchange, Inc., Bats EDGX Exchange, Inc., Financial Industry Regulatory Authority, Inc., NASDAQ BX, Inc., NASDAQ PHLX LLC, The Nasdaq Stock Market LLC, National Stock Exchange, Inc., New York Stock Exchange LLC, NYSE MKT LLC, and NYSE Arca, Inc. (April 21, 2016), *available at* https://www.sec.gov/rules/sro/nms/2016/34-77205.pdf.. *See also* Testimony of Stephen Luparello, Director, Division of Trading and Markets, SEC, before the United States Senate Committee on Banking, Housing, and Urban Affairs Subcommittee on Securities, Insurance, and Investment (March 3, 2016), *available* at https://www.sec.gov/news/testimony/testimony-regulatory-reforms-to-improve-equity-market-structure.html.

[53] *See* Research Note: Equity Market Volatility on August 24, 2015 (December 2015), *available at* https://www.sec.gov/marketstructure/research/equity_market_volatility.pdf.

Implementing Targeted Initiatives to Optimize Equity Market Structure

The Commission is also taking action to address enhanced equity market transparency and disclosure, including our proposal issued in November 2015 to update disclosures by alternative trading systems (ATSs), [54] and I expect a proposal imminently to modernize Rules 605 and 606 of Regulation NMS. Updating Rules 605 and 606 could provide investors with important new information about broker-dealer order handling practices, empowering them to better assess the routing decisions of broker-dealers.

The Commission's proposal on Regulation ATS, issued last November, would require ATS platforms that trade national market system (NMS) stocks to provide significant new transparency with respect their operations. In the years since Regulation ATS was first adopted in 1998, our equity markets have undergone significant change. ATSs are now an important component of our current market structure, fueled by advancements in technology and competing directly with exchanges. Consequently, the number of trading centers has increased substantially, trading activity in NMS stocks is less concentrated, and ATSs collectively now account for approximately 15% of the dollar volume in NMS stocks. This proposal, marking the first-ever major update of Regulation ATS, would require new detailed disclosures about the operation of these platforms and would create a new process for Commission oversight of them.

In addition to enhancing the transparency of our market for investors, the Commission has also advanced measures to improve our core regulatory tools of registration and firm oversight. In March 2015, for example, the Commission proposed important amendments to Rule 15b9-1 to require broker-dealers that engage in off-exchange proprietary trading to become members of a national securities association, which would enhance oversight of active proprietary trading firms.[55] The staff also continues to make progress on recommendations to the Commission to address, among other things, the registration status of certain active proprietary traders, improvements to firms' risk management of trading algorithms, and an anti-disruptive trading rule that would address the use of aggressive, destabilizing trading strategies in vulnerable market conditions.[56]

Assessing Further Data-Driven Enhancements to Equity Market Structure

The Commission's continuing work in market structure is a substantial undertaking that requires updates in technology, and utilization of data and analytics to make informed decisions on enhancing market structure. That means new ways of using existing market data through tools like the Market Information Data Analytics System (MIDAS),[57] and it also means building

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[54] *See* Release No. 34-76474, *Regulation of NMS Stock Alternative Trading Systems* (November 18, 2015), *available at* https://www.sec.gov/rules/proposed/2015/34-76474.pdf.

[55] *See* Release No. 34-74581, *Exemption for Certain Exchange Members* (March 25, 2015), *available at* https://www.sec.gov/rules/proposed/2015/34-74581.pdf.

[56] *See* Chair White Market Structure Framework Speech, *supra* note 43.

[57] Information regarding MIDAS may be found at https://www.sec.gov/marketstructure/midas.html.

new systems to provide even more powerful analytical capabilities for the Commission and our fellow regulators. This past April, the Commission published for comment a proposed national market system plan for the creation of a consolidated audit trail.[58] This is a substantial undertaking and will result in one of the most sophisticated financial databases, providing a full lifecycle of all orders and transactions in our equity and options markets. Final implementation of the consolidated audit trail is a top priority, and I expect the staff to prepare a recommendation for approval of a final plan for Commission action later this year, consistent with Commission Rule 608 under Regulation NMS. After final approval of a plan, Commission Rule 613 requires the selection of a plan processor within two months of approval to build, operate and maintain the consolidated audit trail. Data would be reported by the exchanges and FINRA within one year of Commission approval.

In early 2015, as part of our broader market structure work, the Commission established the Equity Market Structure Advisory Committee to provide a formal mechanism through which the Commission can receive advice and recommendations on key equity market structure issues from a diverse group of experts.[59] The Committee as a whole has since met four times to consider issues such as the operation of Regulation NMS, the impact of access fees and rebates widely used by stock exchanges and the regulatory structure of trading venues, and the impact of various market structure issues on customers. The Committee has established subcommittees to look more closely at specific issues identified by the SEC staff and Committee members before presenting them to the full Committee for discussion and deliberation. The Committee is expected to convene a telephonic meeting on July 8 to receive finalized recommendations from their subcommittees on an access fee pilot program, NMS plan governance, and SRO proposals requiring technology changes. The staff and the Committee will continue to use a variety of tools to ensure both the transparency of the Committee's consideration of issues and input from the full range of investors and other interested market participants, including coordination with our Investor Advisory Committee.

Deepening Oversight of the Fixed Income Markets

Fixed income market structure has long been a focus at the Commission, and the continued impact of technology, regulation, and other forces require us to deepen our oversight. In particular, as I have remarked before, technology in the fixed income markets may not be

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[58] *See* Release No. 34-77724, *Joint Industry Plan; Notice of Filing of the National Market System Plan Governing the Consolidated Audit Trail by BATS Exchange, Inc., BATS-Y Exchange, Inc., BOX Options Exchange LLC, C2 Options Exchange, Incorporated, Chicago Board Options Exchange, Incorporated, Chicago Stock Exchange, Inc., EDGA Exchange, Inc., EDGX Exchange, Inc., Financial Industry Regulatory Authority, Inc., International Securities Exchange, LLC, ISE Gemini, LLC, Miami International Securities Exchange LLC, 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.* (April 27, 2016), *available at* https://www.sec.gov/rules/sro/nms/2016/34-77724.pdf.

[59] Information regarding the committee and its ongoing work can be found at https://www.sec.gov/spotlight/equity-market-structure-advisory-committee.shtml. *See also* Chair Mary Jo White, *Optimizing our Equity Market Structure: Opening Remarks at the Inaugural Meeting of the Equity Market Structure Advisory Committee* (May 13, 2015), *available at* https://www.sec.gov/news/statement/optimizing-our-equity-market-structure.html.

deployed today to achieve all of the benefits it could for investors, including the broad availability of pre-trade pricing information, lower search costs, and greater price competition.[60]

One important step is to ensure that the best execution and pricing disclosure rules for the corporate bond and municipal securities markets are robust and useful to investors, and FINRA and the MSRB have been moving forward on such reforms. At the Commission's urging,[61] the MSRB in December 2014 adopted a best execution rule for the municipal bond market similar to FINRA's best execution rule.[62] And both SROs have since developed and published additional guidance on the best execution obligations of broker-dealers and municipal securities dealers.[63] In 2014, I also urged both FINRA and the MSRB to move forward on markup and markdown disclosure rules, a reform also publicly supported by my fellow Commissioners.[64] Both have advanced proposals and SEC staff has been dedicated to working closely with FINRA and MSRB as the proposals are finalized.

A related effort in these markets is enhancing pre-trade price transparency. Work on this initiative is underway at the SEC. Pre-trade transparency for corporate bonds and municipal securities should remain a critical objective, and the Commission staff continues to work through the challenging issues inherent in such a transformative market structure change. The staff's immediate goal is to develop a recommendation for the Commission's consideration.

The initiatives in these markets also include interagency work on the U.S. Treasury market in the wake of the events of October 15, 2014.[65] One important priority for the Treasury

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[60] *See* Chair Mary Jo White, *Intermediation in the Modern Securities Markets: Putting Technology and Competition to Work for Investors* (June 20, 2014) ("Chair White Fixed Income Speech"), *available at* http://www.sec.gov/News/Speech/Detail/Speech/1370542122012.

[61] *See SEC Report on the Municipal Securities Markets* (July 31, 2012), *available at* http://www.sec.gov/news/studies/2012/munireport073112.pdf.

[62] *See* MSRB Rule G-18 (Best Execution); Release No. 34-73764, *Self-Regulatory Organizations; Municipal Securities Rulemaking Board; Order Granting Approval of a Proposed Rule Change Consisting of Rule G-18, on Best Execution of Transactions in Municipal Securities, and Amendments to Rule G-48, on Transactions with Sophisticated Municipal Market Professionals ("SMMP"), and Rule D-15, on the Definition of SMMP* (December 5, 2014), *available at* https://www.sec.gov/rules/sro/msrb/2014/34-73764.pdf.

[63] *See* MSRB Implementation Guidance on MSRB Rule G-18, on Best Execution (November 2015), *available at* http://www.msrb.org/~/media/Files/MISC/Best-Ex-Implementation-Guidance.ashx?la=en; and FINRA Regulatory Notice 15-46 (November 2015), *available at* https://www.finra.org/sites/default/files/notice_doc_file_ref/Notice_Regulatory_15-46.pdf.

[64] *See, e.g.* Chair White Fixed Income Speech, *supra* note 60; and Commissioners Kara M. Stein and Michael S. Piwowar, *Statement on Edward D. Jones Enforcement Action* (August 13, 2015), *available at* http://www.sec.gov/news/statement/statement-on-edward-jones-enforcement-action.html.

[65] *See Joint Staff Report: The U.S. Treasury Market on October 15, 2014* (July 13, 2015), *available at* https://www.treasury.gov/press-center/press-releases/Documents/Joint_Staff_Report_Treasury_10-15-2015.pdf; Department of Treasury, *Notice Seeking Public Comment on the Evolution of the Treasury Market* (January 22, 2016), *available at* https://www.treasury.gov/press-center/press-releases/Documents/Market%20Structure%20RFI%20Final.pdf.

market is developing a mechanism for post-trade transparency, which systems operated by FINRA and the MSRB already provide in the corporate and municipal markets. Last month, the SEC and Treasury announced the consideration of concrete steps to further enhance post-trade transparency to regulators of the U.S. Treasury cash market, and I look forward to further advancing this effort.[66]

Strengthening Other Critical Market Infrastructures

Clearing agencies provide vital services to both the equity and fixed income markets every day, and it is vital that the clearance and settlement cycle continue to work effectively and efficiently as the markets grow in size and complexity. The Commission has proposed new rules to enhance the oversight of clearing agencies that are deemed to be systemically important or that are involved in complex transactions, such as security-based swaps.[67] Completing these rules is a priority this year in order to guard against systemic risk that can arise in the clearance and settlement system, and provide certainty to market participants, especially those engaged in cross-border activities. I have also directed the staff to develop a recommendation for the Commission's consideration to shorten the settlement cycle,[68] which should yield a number of benefits including reduced counterparty risk and decreased clearing capital requirements. My fellow Commissioners have expressed strong support for this effort,[69] and it is an important measure for the Commission to advance in coordination with the broader SRO and industry efforts underway.

Last year, again with broad support from all of the Commissioners,[70] the SEC also took the first major step in the regulation of transfer agents in decades, issuing an advance notice of proposed rulemaking, concept release, and request for comment on the full regulatory regime.[71]

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[66] *See Statement on Trade Reporting in the Treasury Market* (May 16, 2016), *available at* https://www.sec.gov/news/pressrelease/2016-90.html.

[67] *See* Release No. 34-71699, *Standards for Covered Clearing Agencies* (March 12, 2014), *available at* https://www.sec.gov/rules/proposed/2014/34-71699.pdf.

[68] *See* Letter from Chair White to the Investment Company Institute and the Securities Industry and Financial Markets Association (September 16, 2015), *available at* https://www.sec.gov/divisions/marketreg/chair-white-letter-to-sifma-ici-t2.pdf.

[69] Commissioners Michael S. Piwowar and Kara M. Stein, *Statement Regarding Proposals to Shorten the Trade Settlement Cycle*, (June 29, 2015), *available at* https://www.sec.gov/news/statement/statement-on-proposals-to-shorten-the-trade-settlement-cycle.html.

[70] *See, e.g.*, Chair Mary Jo White, *Beyond Disclosure at the SEC in 2016* (Feb. 19, 2016), *available at* http://www.sec.gov/news/speech/white-speech-beyond-disclosure-at-the-sec-in-2016-021916.html. *See also* Commissioners Michael Piwowar and Kara Stein Statement of Support for the Need to Modernize the Commission's Transfer Agent Rules (June 11, 2015), *available at* http://www.sec.gov/news/statement/statement-of-support-modernize-sec-transfer-agent-rules.html.

[71] *See* Release No. 34-76743, *Transfer Agent Regulations* (December 22, 2015), *available at* https://www.sec.gov/rules/concept/2015/34-76743.pdf.

It is important that this work progress so that the integral work of these market participants continues to serve investors and issuers.

Making Disclosure More Effective for Investors and Issuers

Another important ongoing initiative is our review of the effectiveness of disclosure for investors and issuers. Following the issuance of the Regulation S-K study required by the JOBS Act,[72] I directed the staff to review comprehensively our disclosure regime for corporate issuers and develop specific recommendations for updating the requirements.[73] The goal is for the staff to make recommendations on how to update our rules to facilitate timely, material disclosure by companies, as well as improving shareholders' access to that information.

This is a comprehensive undertaking and the staff is reviewing the disclosure requirements in phases. In the first phase of the review, the staff is focusing on the business and financial disclosures required by periodic and current reports, Forms 10-K, 10-Q and 8-K, and updates to certain Industry Guides, including Guides 3 and 7. The staff is also considering whether disclosure requirements should be scaled for certain categories of issuers, such as smaller reporting companies or emerging growth companies, and, if so, how. In September 2015, the Commission issued a request for comment for certain financial reporting and disclosure requirements in Regulation S-X.[74]

Most recently, in April 2016, the Commission issued a major concept release that seeks input on modernizing certain business and financial disclosure requirements in Regulation S-K for the benefit of investors and companies.[75] We have already received a number of helpful

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[72] *See Report on Review of Disclosure Requirements in Regulation S-K* (December 2013), *available at* https://www.sec.gov/news/studies/2013/reg-sk-disclosure-requirements-review.pdf.

[73] *See* Chair Mary Jo White, *The Path Forward on Disclosure* (October 14, 2013), *available at* https://www.sec.gov/News/Speech/Detail/Speech/1370539878806; and Chair Mary Jo White, *The SEC in 2014* (January 27, 2014), *available at* https://www.sec.gov/News/Speech/Detail/Speech/1370540677500.

[74] See Release No. 33-9929, *Request for Comment on the Effectiveness of Financial Disclosures about Entities other than the Registrant* (September 25, 2015), *available at* https://www.sec.gov/rules/other/2015/33-9929.pdf. Regulation S-X contains disclosure requirements that dictate the form and content of financial statements to be included in filings with the Commission. It addresses both registrant financial statements and financial statements of certain entities other than the registrant. It also requires that domestic issuer financial statements filed with the Commission be prepared in accordance with generally accepted accounting principles.

[75] *See* Release No. 33-10064, *Business and Financial Disclosure Required by Regulation S-K* (April 13, 2016) ("S-K Concept Release"), *available at https://www.sec.gov/rules/concept/2016/33-10064.pdf*. Regulation S-K is the central repository for the Commission's non-financial disclosure requirements. It is intended to foster uniform and integrated disclosure for registration statements under the Securities Act, registration statements under the Securities Exchange Act, and periodic and current reports filed under the Exchange Act. In July 2015, the Commission issued a concept release about possible revisions to audit committee disclosures. *See* Release No. 33-9862, *Possible Revisions to Audit Committee Disclosures* (July 1, 2015), *available at* https://www.sec.gov/rules/concept/2015/33-9862.pdf.

comment letters on the concept release, which discusses many issues and questions that will also serve as a basis for the study of our disclosure requirements mandated by the FAST Act. In a later phase of the project, the staff will review and consider recommendations regarding the governance and compensation disclosures required in proxy statements.

Importantly, the staff is also considering how companies file their disclosures and is exploring alternatives that could enhance the way that investors access the disclosures. This component of our initiative is of vital importance as technology and investors' needs and behavior evolve. In the near term, we are working on changes to sec.gov that would make EDGAR filings more accessible to investors and easier for them to navigate. We also continue to work to improve the technology behind EDGAR and sec.gov, most recently this week by allowing filers to submit eXtensible Business Reporting Language data inline as part of their core filings to facilitate easier access to, and analysis of, information.[76]

Another important new phase of this ongoing review is to expand it to cover investment companies. Last month, I directed staff in the Division of Investment Management to undertake a disclosure effectiveness initiative of their own to consider ways to improve the form, content, and delivery of funds' disclosures.[77] Staff is in the early stages of prioritizing areas of focus, but I expect they will include ways to leverage advances in technology to improve the presentation and delivery of disclosures and ways to enhance disclosure about fund strategies, investments, risks, and fees.

Enhancing Risk Monitoring and Regulatory Safeguards for the Asset Management Industry

We have also already made significant progress on the Commission's major undertaking to enhance risk monitoring and regulatory safeguards for the asset management industry, which I announced in December 2014.[78] This effort, which comprises five core initiatives addressing funds' evolving portfolio composition risks and operational risks, follows the fundamental reforms to money market funds proposed and adopted during my tenure, which will come fully into effect this October.[79]

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[76] *See* Release No. 34-78041, *Order Granting Limited and Conditional Exemption Under Section 36(a) of the Securities Exchange Act of 1934 from Compliance with Interactive Data File Exhibit Requirement in Forms 6-K, 8-K, 10-Q, 10-K, 20-F and 40-F to Facilitate Inline Filing of Tagged Financial Data* (June 13, 2016), *available at* http://www.sec.gov/rules/exorders/2016/34-78041.pdf.

[77] *See* Chair Mary Jo White, *The Future of Investment Company Regulation* (May 20, 2016), *available at* https://www.sec.gov/news/speech/white-speech-keynote-address-ici-052016.html.

[78] *See* Chair Mary Jo White, *Enhancing Risk Monitoring and Regulatory Safeguards for the Asset Management Industry* (December 11, 2014), *available at* https://www.sec.gov/News/Speech/Detail/Speech/1370543677722.

[79] *See* Release No. IC-31166, *Money Market Fund Reform; Amendments to Form PF* (July 23, 2014), *available at* https://www.sec.gov/rules/final/2014/33-9616.pdf.

The Commission has now proposed rules to implement three of the five initiatives I announced in late 2014, all of which I expect will be finalized this year. First, in May 2015, the Commission proposed new rules and forms as well as amendments to its rules and forms to modernize the reporting and disclosure of information by registered investment companies.[80] These proposed rules, if adopted, would require registered funds to provide portfolio-wide and position-level holdings data to the Commission on a monthly basis, as well as report annually on certain census-type information that reflects current information needs. This data would be reported in a structured data format, which would improve the ability of the Commission and the public both to aggregate and analyze information across all funds and to link the reported information with information from other sources. Also in May 2015, the Commission proposed amendments to Form ADV, the primary investment adviser reporting and disclosure form, that would among other things: (1) provide additional information regarding advisers, including information about their separately managed account business; and (2) address issues that staff has identified since the Commission made significant changes to Form ADV in 2011.[81]

To advance the second initiative on liquidity management, in September 2015, the Commission proposed a new rule that would require mutual funds and other open-end investment companies, including ETFs, to adopt and implement liquidity management programs.[82] These funds would also be required to provide enhanced disclosure regarding their liquidity and redemption practices, the methods used by funds to meet redemptions, their committed lines of credit, and interfund borrowing and lending. In addition, mutual funds (except money market funds or ETFs) would be permitted to use "swing pricing,"[83] which would also require additional disclosures.

In December 2015, the Commission advanced the third initiative by proposing a rule that would impose new requirements on the use of derivatives by open and closed-end funds and business development companies.[84] Funds would be required to comply with one of two

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[80] *See* Release Nos. 33-9776; 34-75002; IC-31610, *Investment Company Reporting Modernization* (May 20, 2015), *available at* https://www.sec.gov/rules/proposed/2015/33-9776.pdf.

[81] *See* Release No. IA-4091, *Amendments to Form ADV and Investment Advisers Act Rules* (May 20, 2015), *available at* https://www.sec.gov/rules/proposed/2015/ia-4091.pdf. For example, the proposals would, if adopted, require aggregate information related to assets held and use of borrowings and derivatives in separately managed accounts and provide additional information about an adviser's advisory business, including branch office operations and the use of social media.

[82] *See* Release No. IC-31835, *Open-End Fund Liquidity Risk Management Programs; Swing Pricing; Re-Opening of Comment Period for Investment Company Reporting Modernization Release*, (September 22, 2015), *available at* https://www.sec.gov/rules/proposed/2015/33-9922.pdf.

[83] Swing pricing is the process of reflecting in a fund's net asset value the costs associated with the trading activity of the fund occasioned by shareholders' redemptions and purchases in order to reflect those costs in the prices paid and received by purchasing and redeeming shareholders.

[84] *See* Release No. IC-31933, *Use of Derivatives by Registered Investment Companies and Business Development Companies* (December 11, 2015), *available at* https://www.sec.gov/rules/proposed/2015/ic-31933.pdf.

alternative portfolio limitations designed to limit the amount of leverage that a fund may obtain through derivatives and certain other transactions. In addition, funds would be subject to asset segregation requirements to manage risks associated with derivatives transactions, as well as requirements to establish risk management programs for their derivatives activities.

The SEC staff is working on recommendations to address the two remaining initiatives that I outlined in 2014: transition planning and stress testing. The former, on which I expect a rule proposal to soon be issued soon, would require investment advisers registered with the Commission to create and maintain transition plans to prepare for a major disruption in their business. Staff is also developing a recommendation that the Commission propose new requirements for stress testing by large investment advisers and large investment companies. Such rules would implement, in part, requirements under section 165(i) of the Dodd Frank Act.

Finally, to further promote compliance with our rules in the asset management space, I have asked the staff to prepare a recommendation to the Commission for proposed rules requiring independent compliance assessments for registered investment advisers. The assessments would not replace examinations conducted by OCIE, but would be designed to improve overall compliance by registered investment advisers.

Advancing Personalized Investment Advice Standard of Conduct

Section 913 of the Dodd-Frank Act granted the Commission authority to adopt rules to establish a uniform fiduciary standard of conduct for broker-dealers and investment advisers when providing personalized investment advice about securities to retail customers. As I have stated previously, my evaluation of the differences in the standards that apply to advice under the federal securities laws has led me to conclude that broker-dealers and investment advisers should be subject to a uniform fiduciary standard of conduct when providing personalized investment advice about securities to retail investors. I recognize that this is a complex issue, and that there are significant challenges that will need to be addressed in proposing a uniform fiduciary standard, including how to define the standard, how it would affect current business practices, and the nature of the potential effects on investors, particularly retail investors.

SEC staff has developed a framework for this rulemaking that has been provided to the Commission for its consideration. As part of its analysis in developing its recommendations, the staff is considering, among other things, the SEC staff's 2011 study under Section 913 of the Dodd-Frank Act,[85] the response to the request for information from March 2013,[86] the additional views of investors and other interested market participants, and the potential economic and market impacts. Ultimately, of course, the Commission as a whole will decide whether to

[85] *See Study on Investment Advisers and Broker-Dealers* (January 2011), *available at* https://www.sec.gov/news/studies/2011/913studyfinal.pdf.

[86] *See* Release Nos. 34-69013 and IA-3558, *Duties of Brokers, Dealers, and Investment Advisers* (March 1, 2013), *available at* https://www.sec.gov/rules/other/2013/34-69013.pdf.

proceed with a rulemaking to implement a uniform fiduciary standard and its parameters. And I will continue to discuss all aspects of this issue with my fellow Commissioners as we proceed.

Prioritizing Cybersecurity

Cybersecurity is – as I have said before[87] – one of the greatest risks facing the financial services industry and will be for the foreseeable future. Cybersecurity risks can have far-reaching impacts, and robust and responsible safeguards for market participants and investors' information must be maintained. The Commission has been proactive in publicly prioritizing awareness of cyber risks and in examining and enforcing the rules we oversee that relate to cybersecurity.[88]

Our own regulatory efforts are focused primarily on ensuring that our registered entities have policies and procedures to address the risks posed to their systems and data by cyberattacks. In the asset management space, staff from the Division of Investment Management issued guidance that discussed a number of measures that funds and advisers should consider.[89] We are also are keeping close watch on how public companies are addressing the issue in accordance with the 2011 guidance issued by the Division of Corporation Finance.[90]

On the exam front, the staff is building on its successful "cybersweep" from last year, and will focus on cybersecurity compliance and controls in 2016 as well. [91] This year's efforts will involve more testing to assess firms' preparedness and implementation of firms' procedures and controls. Also, this past November marked the compliance date for most entities covered by Regulation SCI, which, as noted above, covers certain key market participants – including exchanges, large ATSs, clearing agencies, and others.[92] In particular, Regulation SCI requires those entities to have comprehensive policies and procedures in place surrounding their technological systems to make them more resilient. It also requires those entities to report disruptions in their technology systems to the SEC promptly. The first set of exams of SCI entities with respect to these requirements is underway.

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[87] *See, e.g.*, Chair Mary Jo White, *Opening Statement at SEC Roundtable on Cybersecurity* (March 26, 2014), *available at* https://www.sec.gov/News/PublicStmt/Detail/PublicStmt/1370541286468.

[88] General information about these activities can be found at https://www.sec.gov/spotlight/cybersecurity.shtml..

[89] *See Cybersecurity Guidance*, Investment Management Guidance Update No. 2015-02 (Apr. 2015), *available at* https://www.sec.gov/investment/im-guidance-2015-02.pdf.

[90] CF Disclosure Guidance: Topic No. 2, *Cybersecurity* (October 13, 2011), *available at* https://www.sec.gov/divisions/corpfin/guidance/cfguidance-topic2.htm.

[91] *See also* National Exam Program, Risk Alert: Vol. IV, Issue 8, *OCIE's 2015 Cybersecurity Examination Initiative* (Sep. 15, 2015), *available at* https://www.sec.gov/ocie/announcement/ocie-2015-cybersecurity-examination-initiative.pdf.

[92] *See* SCI Adopting Release, *supra* note 44.

Finally, just last month I added a Senior Advisor for Cybersecurity Policy to my staff, who has deep expertise in cybersecurity and will continue to enhance our coordinated approach to cybersecurity policy across the SEC and engage at the highest levels with market participants and other agencies. While all disruptions from cybersecurity events cannot be prevented, we continue to explore ways to ensure that our regulated entities consider the full range of cybersecurity risks to their businesses and consider and use appropriate tools and procedures to prevent breaches, detect attacks, and limit harm.

Strengthening Compliance with Risk-Based Examinations

As I know the Committee appreciates, the Office of Compliance Inspections and Examinations (OCIE) plays a critical role in protecting investors and the integrity of our capital markets. OCIE examiners focus on conducting risk-based examinations of registered entities, including broker-dealers, investment advisers, investment companies, national securities exchanges, SROs, transfer agents, and clearing agencies to evaluate their compliance with applicable regulatory requirements. This work is essential to address deficiencies directly with registrants and, more broadly, to improve industry compliance, detect and prevent fraud, inform policy, and identify risks.

Since the September 2014 hearing, OCIE has continued to bolster its risk-based approach by using data analytics to identify activities that may warrant examination as well as deploying technology to make examinations more efficient and targeted. OCIE's Quantitative Analytics Unit has, for example, developed and continues to improve a National Exam Analytic Tool, which allows examiners to analyze huge amounts of trading data in minutes. These efforts and others have enhanced our ability to reach more registrants, and more effectively use our limited examination resources. In FY 2015, OCIE conducted nearly 2,000 formal examinations of registrants, an increase over each of the prior five fiscal years.

In furtherance of its risk-based approach, OCIE publishes its annual public statement of examination priorities to inform investors and registrants about areas that the staff believes present heightened risk. The examination priorities are selected through a collaborative process in which OCIE's senior management and senior representatives of other SEC Divisions and Offices worked side-by-side to analyze and perform a risk-based assessment of information from a number of sources. In 2016, OCIE's stated priorities include ETFs, fee selection practices at investment advisers and dual registrants, variable annuities, retail retirement issues, clearing agencies, cybersecurity, and Regulation SCI compliance. In March, OCIE created a new Office of Risk and Strategy to consolidate and streamline OCIE's risk assessment, market surveillance, and quantitative analysis teams and provide operational risk management and organizational strategy for OCIE.

Deploying technology and the risk-based approaches as described above is imperative and helpful, but they do not and cannot produce sufficient exam coverage. I remain concerned, as I was in September 2014, that we do not have the resources to adequately examine the vast and growing registered investment adviser population, of which there are more than 12,000. The Commission has therefore taken additional steps to prioritize our limited examination resources to better cover investment advisers. In fiscal year 2015, OCIE conducted more than 1,200 examinations of investment advisers, more examinations than any of the previous five years.

OCIE has also made significant enhancements to its examination program for advisers, including hiring additional industry experts, strengthening its examiner training program and increasing its use of advanced quantitative techniques. However, despite these efforts and in light of rapid growth in the adviser population, OCIE was only able to examine approximately 10% of advisers in fiscal year 2015, representing 30% of assets under management.

This level of coverage cannot be allowed to persist. After exploring a number of additional measures, OCIE is now beginning to transition some resources from its broker-dealer examination program to its program for investment advisers and investment companies. Significantly more resources will still be needed to fulfil our responsibility to investors.

Investing in People and Technology for a Smarter, Stronger Commission

Since I last appeared before this Committee, the Commission has worked hard to enhance its internal operations. The investing public depends on the staff of the Commission and our public systems each day to navigate the securities markets, and it is important that we continue to work to improve the quality of both. For example, we have made increasing investments in information security to improve risk management and monitoring and modernize and secure the SEC's infrastructure. The agency is also engaged in an ongoing, multi-year effort to simplify and optimize the financial reporting process through EDGAR to promote automation and reduce filer burden. With a more modern EDGAR, both the investing public and SEC staff will benefit from having improved access to better data. The steps over the last few years to modernize *SEC.gov* have also continued to improve one of the most widely used federal government websites, making it more flexible, informative, easier to navigate, and secure.

Technology also continues to be the bedrock for much of our ongoing enforcement and examination effort, creating efficiencies and capabilities that were previously impossible. In the last two years, our initiatives have included:

- *Expanding data analytic tools* that assist in the integration and analysis of huge volumes of financial market data, employing algorithms and quantitative models that can lead to earlier detection of fraud or suspicious behavior and ultimately enabling the agency to allocate its resources more effectively. For example, SEC staff has used data analytic (including pattern recognition) tools to, among other things, detect potential fraudulent or manipulative trading, identify financial statement outliers or unusual trends indicative of possible accounting fraud, discover possible money laundering, sift through massive volumes of trading data to detect suspicious trading patterns, and flag higher risk registrants for examination prioritization.

- *Enhancing the Tips, Complaints, and Referral system (TCR)* to bolster its flexibility, configurability, and adaptability. TCR investments will provide more flexible and comprehensive intake, triage, resolution tracking, searching, and reporting functionalities, with full auditing capabilities.

- *Improving enforcement investigation and litigation tracking* to better handle the substantial volume of materials produced during investigations and litigation. Among other initiatives, the SEC needs to build capacity to electronically receive data for tracking and loading (versus the current practice of receiving content via the mail); implement a document management system for Enforcement's internal case files; and revamp the tools used to collect trading data from market participants.

Of course, none of these achievements, including those made possible by enhanced technology, would be possible without the hard work and dedication of the extraordinary women and men who work at the SEC. Our human capital strategy is built to ensure that we continue to attract and retain talented, engaged, and productive employees that reflect the constantly evolving markets we oversee. Since the September 2014 hearing, the Partnership for Public Service named the SEC as the most improved agency in the Best Places to Work in Government annual awards for 2014.[93] And in 2015, the SEC rose to #10 on the Best Places to Work among mid-size agencies list in their annual survey based on the results of our Federal Employee Viewpoint Survey.[94] While these results are encouraging, we remain committed to fostering an even better and stronger workplace to serve the country's investors and its markets.

Conclusion

The Commission's extensive work to protect investors, preserve market integrity, and promote capital formation goes beyond the initiatives and policies I have discussed. But I have tried by example to convey the breadth and importance of the Commission's ongoing efforts and provide a sense of the agency's work both since my time as Chair and since I last testified before this Committee. While more remains to be achieved, I am very proud of the agency's significant accomplishments across its diverse areas of critical responsibilities. For that, I want to thank first and foremost the exceptional staff of the SEC, as well as my fellow Commissioners, present and past. They richly deserve the praise and confidence of investors and the markets.

In closing, I also want to thank the Chairman, the Ranking Member, and this Committee as a whole for your support of the agency's mission. Your continued support will allow the Commission to better protect investors and facilitate capital formation, more effectively oversee the markets and entities we regulate, and continue to build upon the significant progress we have achieved.

I am happy to answer any questions that you may have.

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[93] *See* Partnership for Public Service, *The Big Picture: Profiles of Notable Movers*, *available at* http://bestplacestowork.org/BPTW/rankings/profiles#sec.

[94] *See* Partnership for Public Service, *Best Places to Work Agency Rankings*, *available at* http://bestplacestowork.org/BPTW/rankings/overall/mid.