

Mr. Clayton Goes to Washington

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SEC Chair nominee Jay Clayton's March 23rd hearing before the Senate Banking Committee covered much of the expected ground. In a series of responses designed to avoid controversy, Clayton repeatedly returned to the three core mandates of the SEC – capital formation, investor protection and efficient markets – as touchstones for his future leadership of the Commission, should he be confirmed. Beyond these general areas, Clayton offered few specifics or signals as to how he might steer the Commission during his term as Chair. He did, however, discuss concerns about growing companies finding the U.S. public markets unattractive due to the burdens of being a public company. In response to questions, he also emphasized the need for personal accountability for white collar criminals as a primary means of deterring bad actors. Of particular interest to readers of this blog may be the relative absence of Dodd-Frank discussions from the hearing. Other than emphasizing that he is not targeting any specific provisions for repeal and a promise to continue SEC rulemakings as required by the statute, the possibility of Dodd-Frank reforms were not a hot topic for members of the Committee or the nominee.

Based on these relatively subtle signals, making the public markets more accessible to private companies is likely to be a top priority. Likewise, a continuing commitment to enforcement and perhaps some greater personal accountability for wrongdoings could be on the table, although Clayton specifically declined to discuss the appropriate liability standards for such offenses twice during the hearing. While supporting the need for disclosure, with materiality as the backdrop, he steadfastly avoided expressing a view on whether disclosing political spending should be mandatory, questions that have derailed prior nominations for SEC commissioners.

Below is a list of key topics raised.

Capital formation. Clayton noted that companies are accessing the public markets at a much later stage than in the past “for a variety of reasons.” He believes that over the last 20 years, the United States could have done a much better job in bringing companies to the capital markets, particularly for medium-sized companies during their growth phase. He believes regulatory burdens must be reduced, although he did not provide any specifics. Clayton did attribute some of the shift away from public offerings to more robust private markets, but asserted that broader public markets were good for everyone, because they offer better opportunities for mainstream investors than other types of investments.

Enforcement. Many of the senators’ questions focused on individual accountability in enforcement cases, including whether there should be a strict liability standard. Clayton declined to answer that question, but stressed his belief that prosecution of individuals in the white collar area has a significant deterrent effect, much more so than holding corporations responsible.

Market structure review. Clayton agreed in response to a question that technology will continue to change and influence market structure. As a result, he indicated that we should engage in a “virtually constant assessment” of how our markets are operating, and that he would support a continuation of the Commission’s current efforts in this regard.

Dodd-Frank. Clayton said that he believes Dodd-Frank should be examined, in particular whether the rules already adopted are effective. He stated that he has no specific plans to “attack” any particular provisions, and that he has not discussed the possibility of repealing any particular aspect of the law with anyone. Clayton informed the Committee that if he becomes Chair, he will assess the rulemaking calendar, and that he intends to complete the implementation of the statute. For those carefully watching for an indication of the timing of security-based swap dealer registration, none was to be found.

Regulatory process. In response to several questions about the regulatory process, Clayton agreed that cost-benefit analysis is a critical component of rulemaking, including ongoing consideration of finalized rules to assess whether they

are satisfying their intended objectives. He also expressed a preference for simplicity in regulation wherever possible, noting that complexity creates opportunities for market participants to exploit loopholes and for regulators to exercise a “gotcha” approach to enforcement, each of which can lead to inefficiencies in the market.

Political spending disclosure. The question of whether to require corporate disclosure on political spending has been controversial for other potential SEC commissioners. Clayton noted that his touchstone for disclosure is materiality. He believes that a number of companies are already making this disclosure “because they believe that it is material or may be material,” and shareholders also have access through the shareholder resolution process to ask companies to provide the information.

Cybersecurity board expertise. Recent proposed legislation would require companies to disclose whether or not there is cybersecurity expertise on their boards, and if not, whether that was considered. Clayton acknowledged that there is not enough disclosure about cybersecurity by companies currently. He also believes that investors should know whether companies have considered the issue of whether their boards have expertise or knowledge in cybersecurity.

Activism. Clayton recognized that there is ongoing debate as to whether activism is beneficial or harmful to companies and the market, and whether regulatory mechanisms are necessary to deal with activism.

Pay ratio disclosure. Clayton declined to indicate whether or not he agreed with Acting Chair Piwowar's decision to reopen the comment period on the pay ratio rule, noting that he does not have the background or the staff expertise that Piwowar has that led to his decision.

Legal Assistant Lyla Wasz-Piper contributed to this post.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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