

SEC Chairman Clayton on His Agenda

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SEC Chairman Jay Clayton gave [his first public address](#) yesterday, with some meaningful remarks directed at public company regulations.

The long-term interest of the Main Street Investor (the term is not defined but capitalized in his speech) is the cornerstone of how the SEC will measure whether it is being true to its mission regarding the protection of investors, facilitating capital formation and maintaining markets properly. The Main Street Investor is also characterized as “Mr. and Ms. 401(k)” and it is the SEC’s primary responsibility to ensure that they are informed and have the right opportunities to invest in their future.

Companies Are Weighed Down with Too Much Regulation. Regulatory changes, when viewed in the aggregate rather than incrementally, can “dramatically affect” the markets. The SEC, lawmakers and other regulators have significantly expanded the scope of required disclosures beyond the core concept of materiality, by justifying those actions as providing discrete benefits, directly or indirectly, to “specific shareholders or other constituents.”

Increased Disclosure and Other Burdens Are Making the Public Markets Less Attractive. Instead of looking at regulation piecemeal, the collective disclosure and other requirements may account at least partially for the roughly 50% decline in the total number of U.S.-listed public companies over the last two decades, with arguable benefits. As an example, the median word count of SEC filings has more than doubled, and those documents are becoming harder to read. It is true that many factors influence the decision of whether a company wants to go public, but it is likely also the case that the added regulatory burdens are rendering private markets more appealing. Fewer small and medium-sized public companies mean less liquid trading markets, which ultimately hurt Main Street Investors.

Adopting a Rule Is Only the Beginning. The Commission has a robust process during rule adoption for obtaining public input and performing cost-benefit analysis, but should also review its rules retrospectively to find areas where they are not functioning as intended (“[w]e cannot be shy about being introspective and self-critical”).

The Cost of a Rule Includes the Processes Developed for Compliance. Commission adoption of “vaguely worded rules” leads to either subpar compliance, or too much investment in control systems to demonstrate compliance. He cited to the CEO certification as an example of a situation where the responsibility of the CEO made in that certification will obviously be supported through a chain of command. This could lead to an expensive practice involving third parties that causes financial costs and demands on time to “skyrocket.” While the regulatory approach may be appropriate in some areas, the Commission needs to have a “realistic vision” when adopting rules as to how they will be implemented for compliance.

Companies Must Disclose Cybersecurity Issues, but the SEC Should Be Cautious in Punishing the Victims. Chairman Clayton stressed companies’ obligation to disclose material information about cyber risk and events, and noted that being victim of a sophisticated cyber crime is not an excuse. However, the SEC needs to be “cautious” about “punishing responsible companies” who end up as targets notwithstanding their efforts.

The SEC Needs to Help Private Companies Come to Market. The Chairman reiterated recent actions by the SEC Division of Corporation Finance, which we describe in [our recent memo](#), to make the JOBS Act approach for emerging growth companies more accessible. He also expressly reminded companies that they may request modifications to their financial reporting requirements under Regulation S-X in certain cases and the SEC staff is placing a “high priority” on responding to those requests.

Rulemaking Proposals to Improve Disclosure is in Progress. The Commission has several initiatives underway on modifying disclosure requirements, and he referred to the report that the SEC staff issued last year on modernizing and simplifying Regulation S-K. The staff is making “good progress” on preparing rulemaking proposals based on this report. We previously discussed the SEC concept release [here](#).

In the spirit of bipartisanship, he quoted both Commissioners Piwowar and Stein. He also talked about the need for the SEC to use technology to analyze markets and regulatory filings, the fiduciary rules on investment advice, efforts to reform the market structure and coordinating with other regulators.

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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