Speech

Remarks at the “SEC Speaks” Conference 2017: Remembering the Forgotten Investor

Acting Chairman Michael S. Piwowar

Washington, D.C.

Feb. 24, 2017

Thank you very much, Stephanie [Avakian] and Dave [Grim], for your kind introduction.[1]

Before I begin, I would like to continue a tradition of the SEC Speaks conference and ask that all current staff members of the Securities and Exchange Commission stand so that we may show them our appreciation. SEC employees devote countless hours of hard work and careful thinking in preparing for this event. Next, I would like all those who have ever served at the Commission to rise. I am certain that I speak for my fellow Commissioner, Commissioner Stein, when I express our gratitude for your many years of loyal service to the agency and to our country. Thank you very much.

As is true across the federal government, we are at a time of transition at the SEC. Hopefully we will soon have a Chairman confirmed and the other two vacancies on the Commission filled. In the meantime, the agency remains steadfastly devoted to our core mission, and our work continues.

The Forgotten Investor

In my public statements and speeches, I have stressed the importance of the Commission’s threefold mandate. I do so because all of us—the Commissioners, the staff, market participants, and the public—stand to benefit from a reminder from time to time. Let me continue the refrain: the Commission shall (i) protect investors, (ii) maintain fair, orderly, and efficient markets, and (iii) facilitate capital formation.

Reflecting on our core mission focuses the mind on important questions. *Where* do we see market failures occurring? *What* has Congress authorized us to do about them? *Why* is Commission intervention necessary? *How* can we regulate most effectively? *Which* of our menu of regulatory alternatives is best? Yet, all too often, missing from the equation is another question: *Whom* do we serve?

My theme today is “Remembering the Forgotten Investor,” by which I mean the men and women of our country whom securities regulation is meant to serve and protect but so often has not. I am borrowing here, of course, from the great Yale sociologist of the late-19th and early-20th centuries, William Graham Sumner (1840-1910), who is perhaps best known for coining the term “Forgotten Man” in an essay of the same name.[2] Sumner defined his concept in almost algebraic terms:

> As soon as A observes something which seems to him to be wrong, from which X is suffering, A talks it over with B, and A and B then propose to get a law passed to remedy the evil and help X. Their law always proposes to determine what C shall do for X or, in the better case, what A, B, and C shall do for X.[3]

For Sumner, “C”—not “X”—is the Forgotten Man, or rather, the “man who is never thought of.”[4] He is “the victim of the reformer, social speculator[,] and philanthropist,”[5] even where, as is sometimes the case, actions may be motivated by the very best of intentions. It is the Forgotten Man who is commonly dragooned into someone else's quixotic crusade, sometimes without his knowledge or consent, and often contrary to his interests.

I would like to persuade you that Sumner's formula has something to teach us about the course of securities regulation in our day. Sumner's Forgotten Man is, in our case, the Forgotten Investor, and that forgotten investor has suffered in a number of contexts over the years. I will focus on just a few such examples today, including special-interest disclosure provisions, the "accredited investor" threshold, and civil monetary penalties.

Disclosure and Its Discontents

Disclosure-based securities regulation is the great innovation of our agency. As Justice Louis Brandeis famously wrote, "sunlight is said to be the best of disinfectants; electric light the most efficient policeman."[6] Notice that in Brandeis's epigram, *disclosure* is the disinfectant; *disclosure* is his policeman. Without disclosure, investors have only the most indistinct impressions of a corporation's finances or a mutual fund's portfolio holdings—they perceive the world vaguely, as "through a glass, darkly."[7] But give investors light, and they will have eyes to see.

Imagine, *arguendo*, that we lived in a utopian world in which perfect disclosure of all material information about every company simply existed as a natural feature of the market landscape. Securities markets would be perfectly efficient, with a common state of knowledge immediately and effortlessly transmitted to all investors. Investors would have just what they need—not too much, not too little—to make perfectly informed investment decisions to buy, sell, or hold securities. I need not remind you, however, that we do not live in such a Goldilocks world where the level and content of disclosure is predestined to be "just right."

The Commission thus has an obvious and active role to play in empowering investors through disclosure. Unlike merit-based regimes, our system of disclosure comports well with American traditions of self-reliance, pioneering spirit, and rugged individualism. By arming investors with information, they can evaluate and make investment decisions that support more accurate valuations of securities and a more efficient allocation of capital. Yet we must never lose sight of the legal standard of materiality. As Justice Thurgood Marshall, writing for a unanimous Supreme Court in the seminal case of *TSC Industries v. Northway*, stated, "[t]he question of materiality, it is universally agreed, is an objective one, involving the significance of an omitted or misrepresented fact to a reasonable investor."[8] Justice Marshall expressed his concern that an unnecessarily low standard of materiality and the resulting fear of exposure to substantial liability might cause issuers to "simply bury the shareholders in an avalanche of trivial information—a result that is hardly conducive to informed decision making."[9]

Unfortunately, agreement as to the question of materiality has not been as universal as Justice Marshall supposed. As my good friend, former Commissioner Troy Paredes, noted on this same stage four years ago, an avalanche of immaterial information has been very much in evidence in recent years.[10] Our disclosure regime has repeatedly been coopted for purposes unrelated to investor protection as traditionally understood. Politically motivated disclosure provisions are a manifestation of A and B's taking advantage of C. Or, in Sumner's pithy summation: "Such is the Forgotten Man. He works, he votes, generally he prays—but he always pays—yes, above all, he pays . . . . All the burdens fall on him, or on her . . . ."[11]

The Dodd-Frank Act is rife with examples of burdens ultimately borne by the Forgotten Investor through shareholder money and company resources being expended to provide non-material disclosures—the conflict minerals, pay ratio, and resource extraction provisions to name a few. In an attempt to rationalize our disclosure regime and, in particular to consider impacts on the Forgotten Investor, in recent weeks I have directed the SEC staff to begin reconsideration of two Dodd-Frank mandated rules. Congress and President Trump have vacated a third.

- On January 31, I asked the staff to consider whether its 2014 guidance on the conflict minerals rule[12] “is still appropriate and whether any additional relief [may be] appropriate.”[13] I did so not from any lack of familiarity with or sympathy for the plight of the beleaguered people of the Democratic Republic of the Congo region. As I noted in my public statement, “while visiting Africa last year, I heard first-hand from the people affected by this misguided rule,” which has caused a “*de facto* boycott of minerals from portions of Africa.”[14] I am concerned that “withdrawal from the region may undermine U.S. national security interests by creating a vacuum filled by those with less benign interests.”[15] Nevertheless—whatever the purported benefits of the rule may be—I believe it is categorically wrong to use shareholder assets to fund a humanitarian effort better left to executive agencies with the requisite experiential knowledge.
- Similarly, on February 6, I asked for public comment on any “unexpected challenges” encountered in the implementation of the pay ratio rule,[16] specifically directing the staff “to reconsider the implementation of the rule based on any comments submitted and to determine as promptly as possible whether additional guidance or relief may be appropriate.”[17]
- On February 14, President Trump signed into law a joint resolution of Congress, passed under the Congressional Review Act (the “CRA”), that vacated the Commission’s rule requiring resource extraction disclosures.[18] I have asked the staff to take a fresh look at the rule mandate to determine how we can comply with our statutory obligations in a manner that better aligns with our core mission.

I look forward to working closely with the Division of Corporation Finance and my fellow Commissioners to advance these and other disclosure initiatives in the year to come.

The Accredited Investor Threshold, or How the Other Half Lives

In other contexts, we do not even have to apply Sumner’s Forgotten Man framework to identify those investors whose best interests are being overlooked. Take the registration requirements under the Securities Act of 1933 (the “Securities Act”) and the various exemptions therefrom, including Regulation D. We commonly analyze these rules from the perspective of issuers of securities, with a view to promoting capital formation in the United States. But what if we were to consider these rules from the perspective of the Forgotten Investor?

The Securities Act prohibits the use of any instrument of interstate commerce to offer or sell a security, unless pursuant to a registration statement declared effective by the Commission.[19] It also prohibits “every attempt or offer of, or solicitation of an offer to buy, a security or interest in a security, for value,”[20] defining “offer” broadly to encompass any public statements that might “condition the market” or arouse interest in an issuer.[21] Of course, the Commission has extended certain exemptions from this system, prominently including Regulation D’s safe harbor for private offerings. Regulation D is based on a provision of the Securities Act that exempts “transactions by an issuer not involving any public offering,”[22] an exemption that the Supreme Court has held turns on whether “the particular class of persons affected needs the protection”[23] of the securities laws.

Distinguishing investors who can fend for themselves from those who cannot is a line-drawing exercise fraught with peril. The Commission did just that in 1982 when it adopted Regulation D, dividing the world of private offering investors into two categories: those persons accorded the privileged status of "accredited investor" and those who are not. Like something out of the *ancien régime*, investors lucky enough to earn $200,000 or more in annual income or with a net worth of more than $1 million have available to them myriad investment choices, both public or private. By contrast, *les Misérables* on the other side of the line are severely restricted in their investing options. The $200,000 income test has not been updated since 1982, whereas the net worth test was revised by the Dodd-Frank Act to disallow the counting of home equity,[24] raising the bar even higher to qualify as an "accredited investor."

In my view, there is a glaring need to move beyond the artificial distinction between "accredited" and "non-accredited" investors. I question the notion that non-accredited investors are truly protected by regulations that prevent them from investing in high-risk, high-return securities available only to the Davos jet-set.

Here, I appeal to two well-known concepts from the field of financial economics to show that, in maintaining an "accredited" status in our regulatory structure, we may have forgotten—and in fact disadvantaged—a set of investors. The first is the risk-return tradeoff. Because most investors are risk averse, riskier securities accordingly offer higher returns. Therefore, prohibiting non-accredited investors from investing in high-risk securities amounts to a blanket prohibition on their earning the very highest expected returns.

The second concept is modern portfolio theory. By holding a diversified portfolio of assets, investors reap the benefits of diversification. That is, the risk of the portfolio as a whole is lower than the risk of any individual asset. The correlation of returns is the mathematical key. When adding high-risk, high-return securities to an existing portfolio, so long as the returns from the new securities are not in perfect positive correlation with the existing portfolio, investors may reap higher returns with little to no change in overall portfolio risk. In fact, if the correlations are low enough, the overall portfolio risk can even *decrease*. As such, excluding certain investors from diversification options deprives them of important risk mitigation techniques.

These two basic concepts of economics demonstrate how even a well-intentioned policy of investor protection can do more harm than good, for instance, by exacerbating inequalities of wealth and opportunity.

Whose Pocketbook?—Assessment of Corporate Penalties

I am often asked to describe my thinking when it comes to the assessment of civil monetary penalties on corporations in enforcement actions, especially since I have voted both *for* and *against* corporate penalties. I start from the premise that we must bear the Forgotten Investor in mind when we consider imposing such sanctions.

Take a typical accounting fraud scenario. A financial reporting fraud by the managers of a large company may result in the loss of billions of dollars of market capitalization when the fraud is discovered by the market. This may have widespread direct or indirect effects on millions of shareholders, the value of whose investment plummets. It is entirely appropriate to discipline and punish corporate malefactors who violate our laws, but, when we speak of penalizing a corporation, we must also remember the innocent investors who are so often the primary victims of the fraud. Ultimately, *who* is actually penalized by our penalties?

Of course, every case is different. There are circumstances in which I am fully prepared to support imposition of civil monetary penalties on a corporation. Consider regulated entities, such as broker-dealers or investment advisers, for example. These entities clearly disclose in their corporate filings the degree to which they are regulated and the risk that they may be hit with a penalty if they violate the securities laws. So shareholders are on fair notice—and the market has presumably priced in—that they are investing in a type of entity subject to particular enforcement risks. Similarly, I am generally comfortable with assessing civil monetary penalties in Foreign Corrupt Practices Act cases. According to academic literature, there is evidence that when such violations are revealed to the market, the stock price does not always fall, and may even increase.[25] In sorting through other types of entities and violative conduct, I look to the factors set forth in the Commission's 2006 guidance on penalties[26] and to the excellent event studies and other analyses produced by our Division of Economic and Risk Analysis.

It is all too easy to say that, even in other factual scenarios, corporations that engage in wrongdoing should be penalized where it hurts the most—financially. However, that objective often overlooks a key constituency. Again, the Forgotten Investor, who has already been victimized by corporate fraudsters, is further made to pay for the sins of others.

Three's Company, but Two's a Quorum

Even once we have redoubled our efforts to keep the Forgotten Investor in mind, the Commission is limited in what it can do during this period of transition. For one, as the sole members of the Commission at the moment, Commissioner Stein and I are unfortunately constrained in our ability to discuss the work of the Commission without creating a quorum and becoming subject to the Government in the Sunshine Act.[27] Despite such challenges, the Commission's work moves forward. I am very pleased that we have immediate opportunities to seek to provide meaningful disclosure improvements for the Forgotten Investor.

At our open meeting on March 1, the staff will present four new disclosure recommendations for the Commission to consider:

- **Industry Guide 3:** The last substantive revisions to Industry Guide 3 (Statistical Disclosure by Bank Holding Companies) were undertaken over 30 years ago.[28] The Commission will consider publishing a request for comment to seek public input about disclosures provided by registrants in the financial services industry.
- **Exhibit Hyperlinks and HTML Format:** The Commission will consider introducing a requirement to include a hyperlink to each exhibit listed in the exhibit indices of filings under Item 601 of Regulation S-K (or on Forms F-10 or 20-F). The Commission will also consider whether to require registrants to submit such registration statements and reports to EDGAR in HTML format.
- **Inline XBRL Filing of Tagged Data:** The Commission will consider whether to propose amendments to require the use of "Inline XBRL" format for the submission of operating company financial statement information and mutual fund risk/return summaries. Further, the Commission will consider whether to eliminate the requirement for filers to post Interactive Data Files on their website and whether to terminate the Commission's voluntary program for the submission of financial statement information interactive data.
- **Exchange Act Rule 15c2-12:** Lastly, the Commission will consider whether to propose amendments to Rule 15c2-12. The proposal would amend the list of event notices that a broker, dealer, or municipal securities dealer acting as an underwriter in a primary offering of municipal securities must reasonably determine that an issuer or obligated person has undertaken, in a written agreement or contract for the benefit of holders of the municipal securities, to provide to the

Municipal Securities Rulemaking Board. The proposed amendments would add two event notices relating to certain financial obligations incurred by issuers and obligated persons.

The current two-member Commission has been advancing the interests of the Forgotten Investor in other ways, too. For instance, on February 17, I was pleased to attend a ceremony with our friends and colleagues of the North American Securities Administrators Association to sign an information-sharing agreement as new rules to facilitate intrastate crowdfunding offerings and regional offerings take effect. The agreement not only builds on an already productive relationship between the SEC and state regulators, it also offers additional insights and protections as we help companies grow and create jobs while providing new opportunities to investors.

Finally, the Commission has taken action to prevent members of our nation's Armed Services from joining the ranks of Forgotten Investors, particularly now as the military has begun its transition away from a defined benefit pension to a defined contribution plan. When I was honored to visit the sailors aboard the U.S.S. Carl Vinson recently, it became clear to me that more needs to be done to provide these brave defenders of our liberties with the tools to educate and protect themselves in planning for their retirements. While the SEC already provides military outreach through a variety of mechanisms, I saw an opportunity for us to centralize these efforts and develop new channels of military outreach to meet the investor education needs of the soldiers, sailors, marines, and airmen who so proudly serve our country. I am pleased that our Office of Investor Education has recently announced a position to do just that.

Conclusion

The SEC Speaks conference offers the Commission and members of the securities industry and bar an opportunity to discuss, exchange, and debate ideas. We at the Commission take this opportunity seriously, which is why we have historically devoted so many resources to this event. Throughout the next two days, we will be immersed in our specialized world of jargon and of technical detail. Like Sumner's A and B, we may inadvertently focus so heavily on the problems we perceive in the securities markets and our favored solutions to those problems that we forget the whole reason we are gathered here today: The Forgotten Investor. I therefore leave you with a challenge: In all that you do and say at this year's conference: Remember the Forgotten Investor!

Thank you very much for your kind attention and for your continued devotion to the SEC's mission. Congratulations on your past successes. I look forward to working with you in the year to come.

[1] The views I express today are my own and do not necessarily reflect those of the Commission or my fellow Commissioners.

[2] William Graham Sumner, *The Forgotten Man and Other Essays* (Albert Galloway Keller, ed., 1918).

[3] *Id*. at 466.

[4] *Id*.

[5] *Id*.

[6] Louis D. Brandeis, "What Publicity Can Do," *Harper's Weekly*, Dec. 20, 1913, at 10, *reprinted in* Louis D. Brandeis, *Other People's Money and How the Bankers Use It* 92, 92 (Frederick A. Stokes Co., 1914).

[7] I Corinthians 13:12.

[8] 426 U.S. 438, 445 (1976).

[9] *Id*. at 448-49.

[10] Remarks at The SEC Speaks in 2013, Commissioner Troy A. Paredes, U.S. Securities and Exchange Commission (Feb. 22, 2013), https://www.sec.gov/News/Speech/Detail/Speech/1365171492408.

[11] Sumner, *supra* n. 3, at 491.

[12] Statement on the Effect of the Recent Court of Appeals Decision on the Conflict Minerals Rule, Keith F. Higgins, Director, Division of Corporation Finance, U.S. Securities and Exchange Commission (Apr. 29, 2014), https://www.sec.gov/News/PublicStmt/Detail/PublicStmt/1370541681994.

[13] Reconsideration of Conflict Minerals Rule Implementation, Acting Chairman Michael S. Piwowar, U.S. Securities and Exchange Commission (Jan. 31, 2017), https://www.sec.gov/news/statement/reconsideration-of-conflict-minerals-rule-implementation.html.

[14] *Id*.

[15] *Id*.

[16] Reconsideration of Pay Ratio Rule Implementation, Acting Chairman Michael S. Piwowar, U.S. Securities and Exchange Commission (Feb. 6, 2017), https://www.sec.gov/news/statement/reconsideration-of-pay-ratio-rule-implementation.html.

[17] *Id*.

[18] Pub. L. No. 115-4 (2017).

[19] 15 U.S.C. § 77e (2012).

[20] *Id*. at § 77b(a)(3) (2012).

[21] *See* 22 Fed. Reg. 8359 (Oct. 24, 1957).

[22] 15 U.S.C. § 77d(a)(2) (2012).

[23] *SEC v. Ralston Purina Co.*, 346 U.S. 119 (1953).

[24] Dodd-Frank Wall Street Reform and Consumer Protection Act, § 413(a), Pub. L. No. 111-203 (2010).

[25] *See, e.g.,* The Value of Foreign Bribery to Bribe Paying Firms, Jonathan M. Karpoff, D. Scott Lee, and Gerald S. Martin (June 16, 2015), https://papers.ssrn.com/sol3/papers2.cfm?abstract_id=1573222.

[26] Statement of the Securities and Exchange Commission Concerning Financial Penalties (Jan. 4, 2006), https://www.sec.gov/news/press/2006-4.htm.

[27] *See* 5 U.S.C. § 552b (2012).

[28] Industry Guide 3's last substantive revision, which added disclosures regarding loans and extensions of credit to borrowers in countries experiencing liquidity problems, occurred in 1986. *See* Amendments to Industry Guide Disclosures by Bank Holding Companies, SEC Release No. 33-6677, 51 Fed. Reg. 43594 (Nov. 25, 1986).

Modified: Feb. 24, 2017

Speech

The Markets in 2017: What's at Stake?

Commissioner Kara M. Stein

Washington, D.C.

Feb. 24, 2017

Good morning. As always, it is a pleasure to be part of SEC Speaks. This conference is an important forum that brings together Commission staff, the securities bar, and financial market participants every year to discuss issues of importance to all of us.

Before I begin, I need to remind you that the views I am expressing are my own and do not necessarily reflect the views of the Commission, my fellow Commissioner, or the staff of the Commission.

Throughout this conference you have heard a lot of detail about the policies, rules, and regulations that govern our capital markets. Now, I want to talk about why all of that matters. The markets exist to connect the capital of people who have saved with people who will put that capital to good use building companies and creating jobs. Our policies should reflect that purpose—they should facilitate economic activity in a way that is fair and efficient and that benefits Americans who are saving and investing.

Promoting these goals starts with understanding where the markets are today and where they are headed. In this regard, I am reminded of a Greek philosopher who once said, "change is the only constant." This is very true of our markets. They are in a continual state of change. Financial technology is advancing at a lightening pace. These advances are changing not only trading and back offices, but also how Americans invest and how companies raise capital. It is an exciting time, full of amazing opportunities. But to grasp these opportunities, we must look forward. We cannot drive into the future while looking in the rearview mirror. Instead, we must look at where we are and the road ahead.

Today's Markets

The markets are already significantly different than they were even 10 years ago. For instance, institutional investors now dominate the U.S. equities market. In 2016, institutional investors owned 70 percent of public shares.[1] This is a big increase from even a few years ago.[2] And, some of these institutional investors have become remarkably large. Just a few of our biggest money managers control significant portions of the largest publicly traded companies. Indeed, just three managers hold the largest ownership position in 88 percent of the companies in the S&P 500.[3] This means they manage significant interests in companies that are directly competing with one another. Think about how that could affect the companies.

Exchange-traded products, commonly referred to as ETPs or ETFs, are an important part of the increase in institutional investing. Over the last decade, ETP assets under management have more than tripled.[4] The number of ETPs has grown similarly.[5] Trading in ETP shares also dominates today's equities markets—13 of the 15 most actively traded securities are ETPs.[6] Interestingly, despite the phenomenal growth and diversity of ETPs, these products continue to be governed by a patchwork of rules and exemptions largely developed a decade or more ago.

The growth and diversity of ETPs and other products institutions offer to retail investors provide them with a host of new options and opportunities. ETPs have moved far from their original broad index-tracking origins. And, via a variety of products, retail investors now have access to markets such as volatility, commodities, and interest rates. Retail investors also have an increasing number of ways to access investment advice. Roboadvisers emerged just a few years ago, but their approach to advice has found a place even among many traditional advisers. The result is that investors can now choose among traditional advisers, roboadvisers, and advisers that are a hybrid of the two. As the staff pointed out in guidance published this week, this array of options may open up more affordable access to advice and increase competition. It is indeed a far different world than we lived in 10 years ago.

Trading has also changed. Today, most equity trading is done electronically. And, the fixed income markets are moving rapidly in the same direction. The movement from floor trading to electronic trading brought a number of changes to the equities markets. Trade sizes and prices are now smaller.[7] However, we have also witnessed a number of so-called flash crashes and flash rallies.[8] As the fixed income markets follow the equity markets into electronic trading, we are seeing some of the same changes occur. Fixed income lot sizes are shrinking, trade volume is increasing, and spreads are tightening.[9]

Even the people working in the markets have changed as a result of the move to electronic trading. For example, one major investment bank reportedly reduced its equity traders from 600 to just 2. One third of its employees—9,000 people—are now computer engineers. [10]

The move to electronic trading has also increased the interconnection between securities, products, and marketplaces. When floor trading dominated, it took time for information to become dispersed across securities. Information could not spread faster than the sound of a human voice. Today, information moves much faster. What used to take minutes, now takes only seconds.[11] The markets are more interconnected than ever.

They are also less transparent. More and more trading is being done off exchange and in so-called dark pools. In 2015, roughly one-third of equity trading occurred off-exchange.[12] This move to dark markets affects both price discovery and transparency in the public markets.

Capital raising is seeing a similar move to less transparent venues. Today, more money is raised in unregistered private offerings than in registered offerings.[13] Initial public offerings ("IPOs") are less common.[14] And, overall there are now fewer public reporting companies.[15] Indeed, the shares of some very large companies are not registered with the Commission and, thus, are not subject to public disclosure obligations.[16]

It is important to remember that the effects of securities being offered and traded in the dark are not isolated to a few of the most sophisticated investors. Many of these securities are ultimately owned by millions of Americans through institutional investors. Indeed, the changes in the markets—the rise of institutional investors, the move to private markets, and the evolution of electronic trading—are all closely intertwined.

What do These Changes Mean?

So what do these changes mean? How do they impact the ability of markets to connect those who have saved money with those who will put it to good use building companies and creating jobs?

Let's start with whether the money is being put to its best use. Stock ownership is becoming increasingly concentrated in the hands of a small group of large institutional investors. This raises several questions.

Are the markets allocating money to those who will put it to the best use? Are smaller companies able to access the capital they need to grow and create jobs? Does ownership concentration affect the willingness of companies to compete and invest in innovation? These are all important questions that need answers going forward.

We also must ask whether the market changes are having an effect on the willingness and ability of Americans to provide the capital that these companies need. Disclosure and the resulting transparency have been the foundation of our market system since the Great Depression. Since that time we have relied on the principle that "there cannot be honest markets without honest publicity."[17] Investment and trading are not done in a vacuum—they run on information. Capital finds it best uses when a wide range of participants can fairly weigh relevant, reliable information. So, does the move to opacity impact the effectiveness and efficiency of our capital formation process? Is there sufficient transparency or should we be considering a different foundational principle?

And, lastly, let's talk about the impact of market changes on how money moves through our system. Computerized trading is here to stay. Are the markets sufficiently resilient in this new, faster world? Will the algorithmic traders remain in the markets when we need them the most? Do we have sufficient safeguards against cyberattacks? Or even simple technical glitches?

The Path Forward

These questions reflect an enormous amount of work that needs to be done. Fortunately, some of this work is already underway. The Commission and the exchanges have undertaken various pilot projects to address the mini-flash crashes and flash rallies our markets have been experiencing. Similarly, the Commission and the self-regulatory organizations have started to develop the Consolidated Audit Trail ("CAT") which will allow us to peer into the markets. But, despite all of this, much more needs to be done.

As the ground beneath our feet continues to shift, we need to assess whether our current structure is sufficient to withstand the changes we face. Are there better ways for us to address the challenges of a computerized market? Are anti-manipulation laws passed in an era of floor trading sufficient for an electronic marketplace? Do these laws need to be amended?

We also need to understand why more companies are staying private for longer periods of time. Should we apply enhanced disclosure laws to these private companies? Or perhaps they require a unique set of rules.

Technology is also giving us an opportunity to make information more understandable for investors, while at the same time making it easier for companies to report that information. Rather than rush to eliminate disclosure, we should embrace the chance to use technology to make disclosure better. This would facilitate more efficient capital allocation which would ultimately benefit our entire economy.

We also must address the impact that market changes are having on investors. I urge Commission staff to keep a careful eye on highly complex retail products to ensure that there is adequate information. Further, we should look at whether our rules and laws adequately protect investors harmed by illegal activity. For instance, the amount of money victims lose is often far greater than the gain to wrongdoers. However, the Commission cannot make victims whole because it can only obtain disgorgement, not restitution. Should this change?

These are but a few of the tasks that confront us. The landscape in which we operate is quickly and fundamentally shifting. We too need to change. We cannot address the new world by simply turning the clock backward. Instead, we must look to the future. As President John F. Kennedy said: "Change is the law of life. And those who look only to the past or present are certain to miss the future."[18] We cannot miss the future. Our financial markets are too important. They help companies raise capital. They create jobs. And, they help Americans save for their children's education and their own retirements. The markets are vital to our economy. And, we need to help them adapt to meet the demands of a new and ever changing world.

I look forward to working with all of you on these very important issues.

Thank you.

[1] During the 2016 proxy season, institutional investors owned 73% of large cap shares, 77% of mid-cap shares, 68% of small cap shares, and 33% of microcap shares. Broadridge & PwC, ProxyPulse: 2016 Proxy Season Review (2016), *available at* http://media.broadridge.com/documents/Broadridge-ProxyPulse-3rd-Edition-2016.pdf.

[2] The Conference Bd., The 2010 Institutional Investment Report (2010).

[3] Jan Fichtner, *et al.*, Hidden Power of the Big Three? Passive Index Funds, Re-Concentration of Corporate Ownership and New Financial Risk (CORPNET, Univ. of Amsterdam, Working Paper, 2017).

[4] Total net assets of ETFs were $608 million in 2007 and $2.1 trillion in 2015. Investment Company Institute, 2016 Investment Company Fact Book, *available at* https://www.ici.org/pdf/2016_factbook.pdf.

[5] There were 629 ETFs in 2007 and 1,594 in 2015. *Id.*

[6] Dani Burger, Stocks Are No Longer the Most Actively Traded Securities in Stock Markets, Bloomberg (Jan. 12, 2017), *available at* https://www.bloomberg.com/news/articles/2017-01-12/stock-exchanges-turn-into-etf-exchanges-as-passive-rules-all.

[7] James Angel, *et al*., Equity Trading in the 21st Century, USC Marshall School of Business Research Paper Series, Working Paper FBE 09-10 (2010), *available at* https://www.sec.gov/spotlight/emsac/equity-trading-in-the-21st-century.pdf.

[8] *See, e.g*., CFTC & SEC, Findings Regarding the Market Events of May 6, 2010 (2010), *available at* https://www.sec.gov/news/studies/2010/marketevents-report.pdf; U.S. Dep't of Treasury *et al*., The U.S. Treasury Market on October 15, 2014 (2015), *available at* https://www.treasury.gov/press-center/press-releases/Documents/Joint_Staff_Report_Treasury_10-15-2015.pdf.

[9] Bruce Mizrach, Analysis of Corporate Bond Liquidity, FINRA Office of the Chief Economist Research Note, *available at* http://www.finra.org/sites/default/files/OCE_researchnote_liquidity_2015_12.pdf.

[10] Nanette Byrnes, As Goldman Embraces Automation, Even the Masters of the Universe Are Threatened, MIT Technology Review (Feb. 7, 2017), *available at* https://www.technologyreview.com/s/603431/as-goldman-embraces-automation-even-the-masters-of-the-universe-are-threatened/?set=603585.

[11] *See, e.g.,* Austin Gerig, High-Frequency Trading Synchronizes Prices in Financial Markets, DERA Working Paper Series, *available at* https://www.sec.gov/dera/staff-papers/working-papers/dera-wp-hft-synchronizes.pdf.

[12] Changing Business Models of Stock Exchanges and Stock Market Fragmentation, OECD Business and Finance Outlook (2016), *available at* https://www.oecd.org/daf/ca/BFO-2016-Ch4-Stock-

Exchanges.pdf.

[13] Scott Bauguess *et al.,* Capital Raising in the U.S: An Analysis of the Market for Unregistered Securities Offerings, 2009-2014 (2015), *available at* https://www.sec.gov/dera/staff-papers/white-papers/unregistered-offering10-2015.pdf (finding that in 2014, $2.1 trillion was raised through private offerings and $1.35 trillion was raised via registered offerings).

[14] EY, Why Are More Companies Staying Private? Meeting of SEC Advisory Committee on Small and Emerging Companies (2017), *available at* https://www.sec.gov/info/smallbus/acsec/giovannetti-presentation-acsec-021517.pdf; Xiaohui Gao *et al.,* Presentation to the SEC Advisory Committee on Small and Emerging Companies (2012), *available at* https://www.sec.gov/info/smallbus/acsec/acsec-090712-ritter-slides.pdf.

[15] Craig Doidge *et al.,* The U.S Listing Gap, National Bureau of Economic Research Working Paper No. 21181 (2015), *available at* http://www.nber.org/papers/w21181.

[16] There are nearly 200 private U.S. companies with a valuation of over $1 billion. These so-called "unicorns" have a combined valuation of nearly $700 billion. The Unicorn List: Current Private Companies Valued at $1B and Above, CB Insights (updated daily), *available at* https://www.cbinsights.com/research-unicorn-companies.

[17] H.R. Rep. 73-1383, 73rd Cong., 2nd Sess. (Apr. 27, 1934).

[18] John F. Kennedy, Address in the Assembly Hall at the Paulskirche (1963), *available at* http://www.presidency.ucsb.edu/ws/?pid=9303.

Modified: Feb. 24, 2017

Press Release

SEC, NASAA Sign Info-Sharing Agreement for Crowdfunding and Other Offerings

FOR IMMEDIATE RELEASE
2017-50

Washington D.C., Feb. 17, 2017 — The Securities and Exchange Commission and the North American Securities Administrators Association today signed an information-sharing agreement as new rules to facilitate intrastate crowdfunding offerings and regional offerings take effect.

The agreement signed by the SEC and NASAA is intended to facilitate the sharing of information to ensure that the new exemptions are serving their intended purpose of facilitating access to capital for small businesses. Under the memorandum of understanding (MOU), federal and state securities regulators will be better able to monitor the effects of the new rules and also guard against fraud.

The MOU was signed by SEC Acting Chairman Michael S. Piwowar and Mike Rothman, Minnesota Commissioner of Commerce and President of NASAA, which represents state securities administrators.

"The agreement not only builds on an already productive relationship between the SEC and state regulators, it also offers additional insights and protections as we help companies grow and create jobs while providing new opportunities to investors," said Acting Chairman Piwowar.

"The agreement not only b
on an already productive relat
between the SEC and state
regulators, it also offers additic
insights and protections as we
companies grow and create jc
while providing new opportun
investors.
-Acting Chairman Piwowar

"This agreement will strengthen collaboration among state and federal securities regulators to help expand small-business investment opportunities while also protecting investors," said Rothman. "Ongoing dialogue is essential to carry out our responsibilities going forward. With this MOU in place, we have an opportunity to share information that will bolster our efforts to support small business capital formation and prevent fraud."

Under the new rules, companies will have more flexibility to engage in intrastate offers through websites and social media without having to register their offering with the federal government. Companies now can also raise up to $5 million per year through other amended rules, which could facilitate the development of regional offering exemptions at the state level to permit companies to raise from investors in a specific region. The previous limit was $1 million.

New JOBS Act rules went into effect in 2015 and 2016. New amendments to facilitate regional offerings went into effect in January and amendments to provide more flexibility for intrastate crowdfunding offerings will go into effect in April. These amendments are intended to facilitate greater access to capital for entrepreneurs that may not have been able to otherwise access capital using other alternatives. The MOU will increase the regulators' ability to share data to better monitor implementation of the new rules and guard against fraud.

NASAA President Mike Rothman (L) and SEC Acting Chairman Michael Piwowar sign MOU.

###

Related Materials

- SEC Acting Chairman Michael Piwowar's Remarks
- Memorandum of Understanding

Press Release

SEC Approves Rules to Ease Investor Access to Exhibits in Company Filings

FOR IMMEDIATE RELEASE
2017-55

Washington D.C., March 1, 2017 — The Securities and Exchange Commission today voted to adopt rule and form amendments to make it easier for investors and other market participants to find and access exhibits in registration statements and periodic reports that were originally provided in previous filings.

The amendments will require issuers to include a hyperlink to each exhibit in the filing's exhibit index. Currently, someone seeking to retrieve and access an exhibit that has been incorporated by reference must review the exhibit index to determine the filing in which the exhibit is included, and then must search through the registrant's filings to locate the relevant filing.

"As the SEC looks for new ways to modernize financial disclosures, one of the easiest things we can do is add hyperlinks that automatically direct users to additional information on our EDGAR system," said SEC Acting Chairman Michael Piwowar. "We are so accustomed to clicking hyperlinks on basically every website we visit, this commonsense solution will make life simpler for a lot of people."

The final rules will take effect on September 1, 2017.

* * *

FACT SHEET

SEC Open Meeting

March 1, 2017

Highlights

The amendments require registrants that file registration statements or reports subject to the exhibit requirements under Item 601 of Regulation S-K, or that file Forms F-10 or 20-F, to include a hyperlink to each exhibit listed in the exhibit index of these filings, and to submit such registration statements and reports on EDGAR in HyperText Markup Language (HTML) format.

Specifically:

- Registrants will be required to include a hyperlink to each exhibit identified in the exhibit index, unless the exhibit is filed in paper pursuant to a temporary or continuing hardship exemption under Rules 201 or 202 of Regulation S-T, or pursuant to Rule 311 of Regulation S-T. This requirement will apply to the forms for which exhibits are required under Item 601 of Regulation S-K as well as Forms F-10 and 20-F. The final rules, however, will exclude exhibits that are filed with Form ABS-EE and exhibits filed in the eXtensive Business Reporting language (XBRL).
- Registrants will be required to file in HTML format the registration statements and reports subject to

the exhibit filing requirements under Item 601 of Regulation S-K, as well as Forms F-10 and 20-F, because the text-based American Standard Code for Information Interchange (ASCII) format cannot support functional hyperlinks. While the affected registration statements and reports will be required to be filed in HTML, registrants may continue to file in ASCII any schedules or forms that are not subject to the exhibit filing requirements under Item 601, such as proxy statements, or other documents included with a filing, such as an exhibit.

What's Next

The final rules will provide a longer compliance date for non-accelerated filers and smaller reporting companies and for certain filings on Form 10-D. Under the final rules:

- Non-accelerated filers and smaller reporting companies that submit filings in ASCII will not have to comply with the final rules until September 1, 2018.
- The compliance date for any Form 10-D filing that will require a hyperlink to an exhibit filed with Form ABS-EE will be delayed until SEC staff completes programming changes to EDGAR that will allow registrants to include the Form 10-D and Form ABS-EE in a single submission so that the required exhibit hyperlinks can be created at the time the Form 10-D is filed. The SEC will publish a notice in the Federal Register and on the SEC website announcing the compliance date for those Form 10-D filings.

###

Related Materials

- Final Rule