Testimony on "Wall Street Reform: Oversight of Financial Stability and Consumer and Investor Protections"
by
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Chairman Johnson, Ranking Member Crapo, and members of the Committee:

Thank you for inviting me to testify on behalf of the Securities and Exchange Commission regarding our ongoing implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act" or "Act"). We appreciate the opportunity to share with you the steps we have been taking and the procedures we have followed.

As you know, the Dodd-Frank Act added significant new responsibilities to the SEC's portfolio, as well as creating new tools for use in executing those and other responsibilities. To date, the Commission has made substantial progress in writing the huge volume of new rules the Act directs, as well as in conducting the various studies required by the Act. Of the more than 90 Dodd-Frank provisions that require SEC rulemaking, the SEC has proposed or adopted rules for over 80 percent of them, and also has finalized 17 of the more than 20 studies and reports that the Act directs us to complete. While this has been a challenge, the considerable progress the Commission has made is a direct result of the thoughtful, thorough, and professional efforts of our staff, whose efforts in fulfilling the Dodd-Frank Act mandates have come in addition to carrying their normal workloads.

My testimony today will provide an overview of the Commission's Dodd-Frank Act activities, emphasizing our accomplishments over the past year.

Hedge Fund and Other Private Fund Adviser Registration and Reporting

The Dodd-Frank Act mandated that the Commission require private fund advisers (including hedge and private equity fund advisers) to confidentially report information about the private funds they manage for the protection of investors or for the assessment of systemic risk by the Financial Stability Oversight Council ("FSOC"). On October 31, 2011, in a joint release with the Commodity Futures Trading Commission ("CFTC"), the Commission adopted a new rule that requires hedge fund advisers and other private fund advisers registered with the Commission periodically to report systemic risk information on a new form, "Form PF".[1]

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[1] *See* Release No. IA-3308, *Reporting by Investment Advisers to Private Funds and Certain Commodity Pool Operators and Commodity Trading Advisors on Form PF* (October 31, 2011), http://www.sec.gov/rules/final/2011/ia-3308.pdf.

Under the rule, registered investment advisers managing at least $150 million in private fund assets must periodically file Form PF. Both the amount of information required to be reported and the frequency with which Form PF must be filed are scaled to the size of the adviser and the nature of its advisory activities.[2] This scaled approach will provide FSOC and the Commission with a broad view of the industry while relieving smaller advisers from much of the reporting burden. In addition, the reporting requirements are tailored to the types of funds an adviser manages and the potential risks those funds may present, meaning that an adviser will respond only to questions relevant to its business model. The Dodd-Frank Act provides special confidentiality protections for this data. To ensure that the data is handled in a manner that reflects its sensitivity and statutory confidentiality protections, a Steering Committee composed of senior officers from various Divisions and Offices within the Commission has been established to implement a consistent approach regarding the access to, and use, sharing, and data security of, information collected through Form PF. The Steering Committee is also working with FINRA (the contractor that operates the Form PF filing system) and the Office of Financial Research (the FSOC entity that will receive and use the data on behalf of FSOC) to implement appropriate controls to protect it.

The largest advisers to liquidity funds and hedge funds began filing Form PF reports in the summer of 2012. As of December 31, 2012, the Commission received filings from 228 registered advisers of private funds. Smaller private fund advisers generally must begin filing with the Commission in March and April of this year.

In addition to Form PF, the Commission has implemented a number of other Dodd-Frank provisions that serve to enhance oversight of private funds advisers. These enable, for the first time, regulators and investors to have a more comprehensive view of the private fund universe and the investment advisers managing those assets.

- In June 2011, the Commission adopted rules that require the registration of, and reporting by, advisers to hedge funds and other private funds and other advisers previously exempt from SEC registration. As a result, the number of private fund advisers registered with the Commission – advisers that manage one or more private funds – increased significantly. As of January 2, 2013, the number of SEC- registered private fund advisers had increased by more than 50% from the effective date of the Dodd-Frank Act to 4,020 advisers. These advisers now represent approximately 37% of all SEC- registered investment advisers and collectively manage over 24,000 private funds with total assets of $8 trillion.[3]

[2] To the extent an investment adviser is currently required to file Form PF, examination staff review the individual filings prior to conducting investment adviser examinations. The review of Form PF assists in identifying additional risk areas and may highlight particular funds for focus during the exam.

[3] For more information on investment advisers registered with the Commission and advisers required to report information to the Commission after the Dodd-Frank Act, as well as the private funds they manage, see *Dodd-Frank Act Changes to Investment Adviser Registration Requirements*, http://www.sec.gov/divisions/investment/imissues/df-iaregistration.pdf.

- Concurrently, the Commission adopted rules to implement new adviser registration exemptions created by the Dodd-Frank Act. The new rules implement exemptions for: (i) advisers solely to venture capital funds; (ii) advisers solely to private funds with less than $150 million in assets under management in the United States; and (iii) certain foreign advisers without a place of business in the U.S. and with only *de minimis* U.S. business.[4]

- These new rules also implement the Dodd-Frank requirement for public reporting by investment advisers to venture capital funds and others that are exempt from SEC registration.

- The rules also reallocate regulatory responsibility to state securities authorities for advisers with between $25 million and $100 million in assets under management.[5] To facilitate the reallocation of regulatory responsibility, the Commission issued an order in February 2013 cancelling the registrations of certain SEC-registered investment advisers no longer eligible to remain registered.[6]

- In June 2012, the Commission also adopted a new rule defining "family offices," a group that historically has not been required to register as advisers and that is now excluded by rule from the Investment Advisers Act of 1940 ("Advisers Act") definition of an investment adviser.[7]

- In February 2012, the Commission adopted amendments to the rule that permits investment advisers to charge performance fees to "qualified clients."[8] The amendments codified the Commission's 2011 inflation adjustments to the net worth and assets-under-management thresholds that clients must satisfy for the adviser to charge these fees. The amendments also excluded the value of a person's primary residence from the rule's net worth test and provided that, as required by the Dodd-Frank Act, the Commission will issue an order every five years adjusting the rule's dollar amount thresholds for inflation.

Since the Act became effective, approximately 2,250 formerly SEC registered advisers have transitioned to state registration and approximately 1,500 advisers to hedge funds and

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[4] *See* Release No. IA-3222 *Exemptions for Advisers to Venture Capital Funds, Private Fund Advisers With Less Than $150 Million in Assets Under Management, and Foreign Private Advisers* (June 22, 2011), http://www.sec.gov/rules/final/2011/IA-3222.pdf.

[5] *See* Release No. IA-3221, *Rules Implementing Amendments to the Investment Advisers Act* (June 22, 2011), http://www.sec.gov/rules/final/2011/ia-3221.pdf.

[6] *See* Release No. IA-3547, *Order Cancelling Registrations of Certain Investment Advisers Pursuant to Section 203(h) of the Investment Advisers Act of 1940* (February 6, 2013), http://www.sec.gov/rules/other/2013/ia-3547.pdf.

[7] *See* Release No. IA-3220, *Family Offices* (June 22, 2011), http://www.sec.gov/rules/final/ia-3220.pdf.

[8] *See* Release No. IA-3372, *Investment Adviser Performance Compensation* (February 15, 2012), http://www.sec.gov/rules/final/2012/ia-3372.pdf.

private equity funds have registered with the Commission. These new adviser registrants report over $3 trillion in assets under management, while those that transitioned to state registration manage about $115 billion. Most of these new registrants had never been registered, regulated, or examined and many have complex business models, investment programs and trading strategies. Commission staff, through our National Exam Program, has developed and begun implementing a program for these new advisers which includes outreach, examination, and, ultimately, where appropriate, written reports highlighting exam findings.

Whistleblower Program

Pursuant to Section 922 of the Dodd-Frank Act, the SEC established a whistleblower program to pay awards to eligible whistleblowers that voluntarily provide the agency with original information about a violation of the federal securities laws that leads to a successful SEC enforcement action. The SEC's Office of the Whistleblower filed its second Annual Report to Congress on November 15, 2012, detailing the Office's activities during the fiscal year.[9] As detailed in the Annual Report, during fiscal year 2012 the Commission received 3,001 tips from whistleblowers in the U.S. and 49 other countries. Among other things, the Office (1) regularly communicates with whistleblowers, returning over 3,050 phone calls to the public hotline during fiscal year 2012; (2) identifies and tracks whistleblower tips that may lead to enforcement actions; (3) reviews and processes applications for whistleblower awards; (4) facilitates meetings between whistleblowers and SEC Enforcement staff; and (5) provides extensive guidance to Enforcement staff on various aspects of the program, including proper handling of confidential whistleblower identifying information.

The high quality information that we have been receiving from whistleblowers has, in many instances, allowed our investigative staff to work more efficiently and permitted us to better utilize agency resources.

In August, 2012, the Commission made its first award under the whistleblower program.[10] We expect future payments to further increase the visibility and effectiveness of this important Enforcement initiative.

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[9] *Annual Report on the Dodd-Frank Whistleblower Program Fiscal 2012* (November 2012), http://www.sec.gov/about/offices/owb/annual-report-2012.pdf.

[10] A whistleblower who helped the Commission stop a multi-million dollar fraud received an award of 30 percent of the amount collected in the Commission's enforcement action against the perpetrators of the scheme, the maximum amount permitted by the Act. The award recipient in this matter submitted a tip concerning the fraud and then provided documents and other significant information that allowed the Commission's investigation to move at an accelerated pace and ultimately led to the filing of an emergency action in federal court to prevent the defendants from ensnaring additional victims and further dissipating investor funds. *See In the Matter of the Claim for Award,* Release No. 34-67698 (August 21, 2012), http://www.sec.gov/rules/other/2012/34-67698.pdf, and *In the Matter of the Claim for Award,* SEC Release No. 34-67699 (August 21, 2012), http://www.sec.gov/rules/other/2012/34-67699.pdf.

OTC Derivatives

Among the key provisions of the Dodd-Frank Act are those that establish a new oversight regime for the over-the counter ("OTC") derivatives marketplace. Title VII of the Act requires the Commission to regulate "security-based swaps" and to write rules that address, among other things, mandatory clearing, reporting and trade execution, the operation of clearing agencies, data repositories and trade execution facilities, capital and margin requirements and business conduct standards for dealers and major market participants, and public transparency for transactional information. Among other things, such rules are intended to:

- Facilitate the centralized clearing of swaps, with the intent of reducing counterparty and systemic risk;
- Increase market transparency;
- Increase security-based swap transaction disclosure; and
- Address potential conflict of issues relating to security-based swaps.

Title VII Implementation Generally

The Commission has proposed substantially all of the core rules required by Title VII. In addition, the Commission has adopted a number of final rules and interpretations, provided a "roadmap" to implementation of Title VII, and taken other actions to provide legal certainty to market participants during the implementation process. In implementing Title VII, Commission staff is in regular contact with the staffs of the CFTC, the Board of Governors of the Federal Reserve System ("Board") , and other federal financial regulators, and in particular has consulted and coordinated extensively with CFTC staff.

Adoption of Key Definitional Rules

In July 2012, the Commission adopted final rules and interpretations jointly with the CFTC regarding key product definitions under Title VII.[11] This effort follows the Commission's work on the entity definitions rules, which the Commission adopted jointly with the CFTC in April 2012.[12] The completions of these joint rulemakings are foundational steps toward the complete implementation of Title VII.

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[11] *See* Release No. 33-9338, *Further Definition of "Swap," "Security-Based Swap," and "Security-Based Swap Agreement"; Mixed Swaps; Security-Based Swap Agreement Recordkeeping* (July 18, 2012) http://www.sec.gov/rules/final/2012/33-9338.pdf.

[12] *See* Release No. 34-66868, *Further Definition of "Swap Dealer," "Security-Based Swap Dealer," "Major Swap Participant," "Major Security-Based Swap Participant" and "Eligible Contract Participant* (April 27, 2012) http://www.sec.gov/rules/final/2012/34-66868.pdf.

The July joint rulemaking addressed certain product definitions and further defined the key terms "swap," "security-based swap," and "security-based swap agreement." It also adopted rules regarding the regulation of "mixed swaps" and the books and records requirements for security-based swap agreements. The April joint rulemaking further defined the key terms "swap dealer" and "security-based swap dealer," providing guidance as to what constitutes dealing activity, and distinguishing dealing from non-dealing activities such as hedging. The rulemaking also implemented the Dodd-Frank Act's statutory *de minimis* exception to the security-based swap dealer definition in a way tailored to reflect the different types of security-based swaps. Additionally, the rulemaking implemented the Dodd-Frank Act's "major security-based swap participant" definition through the use of three objective tests.

While foundational, these final rules did not trigger compliance with the other rules the Commission is adopting under Title VII. Instead, the compliance dates applicable to each final rule will be set forth in the adopting release for the applicable rule. In this way, the Commission is better able to provide for an orderly implementation of the various Title VII rules.

Adoption of Rules and Other Action related to Clearing

In addition to the key definitional rules, the Commission has adopted rules under Title VII relating to clearing infrastructure. In October 2012, the Commission adopted a rule that establishes operational and risk management standards for clearing agencies, including clearing agencies that clear security-based swaps.[13] The rule, discussed in more detail below, is designed to help ensure that clearing agencies will be able to fulfill their responsibilities in the multi-trillion dollar derivatives market as well as in more traditional securities markets.

In June 2012, the Commission adopted rules that establish procedures for its review of certain actions undertaken by clearing agencies.[14] These rules detail how clearing agencies will provide information to the Commission about the security-based swaps the clearing agencies plan to accept for clearing, which will then be used by the Commission to aid in determining whether those security-based swaps are required to be cleared. The adopted rules also include rules requiring clearing agencies that are designated as "systemically important" under Title VIII of the Dodd-Frank Act to submit advance notice of changes to their rules, procedures, or operations if the changes could materially affect the nature or level of risk at those clearing agencies.

In addition, in December 2012, the Commission issued an order providing exemptive relief in connection with a program to commingle and portfolio margin customer positions in

[13] *See* Release No. 34-68080, *Clearing Agency Standards* (October 22, 2012), http://www.sec.gov/rules/final/2012/34-68080.pdf.

[14] *See* Release No. 34-67286, *Process for Submissions for Review of Security-Based Swaps for Mandatory Clearing and Notice Filing Requirements for Clearing Agencies; Technical Amendments to Rule 19b-4 and Form 19b-4 Applicable to All Self-Regulatory Organizations* (June 28, 2012), http://www.sec.gov/rules/final/2012/34-67286.pdf.

cleared credit default swaps which include both swaps and security-based swaps.[15] Portfolio margining may be of benefit to investors and the market by, among other things, promoting greater efficiency in clearing, helping to alleviate excessive margin calls, improving cash flow and liquidity, and reducing volatility. Previously, in March 2012, the Commission had adopted rules providing exemptions under the Securities Act of 1933 ("Securities Act"), the Securities Exchange Act of 1934 ("Exchange Act"), and the Trust Indenture Act of 1939 for security-based swaps transactions involving certain clearing agencies satisfying certain conditions.[16]

Adoption of Rules Related to Reporting

In 2010, the Commission adopted an interim final temporary rule regarding the reporting of certain information relating to outstanding security-based swap transactions entered into prior to the date of enactment of the Dodd-Frank Act.[17] In 2011, we also readopted certain of our beneficial ownership rules to preserve their application to persons who purchase or sell security-based swaps.[18]

Issuance of Implementation Policy Statement

In addition to its work to propose and adopt Title VII rules, the Commission issued a policy statement in June 2012, describing and requesting public comment on the order in which it expects to require compliance by market participants with the final Title VII rules.[19] The Commission's approach aims to avoid the disruption and cost that could result if compliance with all of the rules were required simultaneously or haphazardly. More generally, the policy statement is part of our overall commitment to making sure that market participants know what the "rules of the road" are before requiring compliance with those rules.

The implementation policy statement is divided into five broad categories of final rules to be adopted by the Commission and explains how the compliance dates of these rules would be sequenced in relative terms by describing the dependencies that exist within and among the categories. The statement emphasizes that those subject to the new regulatory requirements arising from these rules will be given adequate, but not excessive, time to come into compliance with them.

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[15] *See* Release No. 34-68433, *Order Granting Conditional Exemptions Under the Securities Exchange Act of 1934 in connection with Portfolio Margining of Swaps and Security-Based Swaps* (December 14, 2012), http://sec.gov/rules/exorders/2012/34-68433.pdf.

[16] *See* Release No. 33-9308, *Exemptions for Security-Based Swaps Issued by Certain Clearing Agencies* (March 30, 2012), http://www.sec.gov/rules/final/2012/33-9308.pdf.

[17] *See* Release No. 34-63094, *Reporting of Security-Based Swap Transaction Data* (October 13, 2010), http://www.sec.gov/rules/interim/2010/34-63094.pdf.

[18] *See* Release No. 34-64628, *Beneficial Ownership Reporting Requirements and Security-Based Swaps* (June 8, 2011), http://www.sec.gov/rules/final/2011/34-64628.pdf.

[19] *See* Release No. 34-37177, *Statement of General Policy on the Sequencing of the Compliance Dates for Rules Applicable to Security-Based Swaps* (June 11, 2012), http://www.sec.gov/rules/policy/2012/34-67177.pdf.

The statement also discusses the timing of the expiration of temporary relief the Commission previously granted security-based swap market participants from certain provisions of the federal securities laws. The expiration of much of this relief is tied to the effective or compliance dates of certain rules to be adopted pursuant to Title VII.

Market participants have provided comments on the sequencing set out in the policy statement, and we are taking those into account as we work toward completing the Title VII adoption process.

Provision of Legal Certainty

Consistent with our commitment to an orderly Title VII implementation process, the Commission has taken a number of steps to provide legal certainty and avoid unnecessary market disruption that might otherwise have arisen as a result of final rules not having been adopted by the July 16, 2011 effective date of Title VII. Specifically, we have:

- Provided guidance regarding which provisions in Title VII governing security-based swaps became operable as of the effective date and provided temporary relief from several of these provisions;[20]

- Provided guidance regarding – and, where appropriate, interim exemptions from – the various pre-Dodd-Frank provisions that otherwise would have applied to security-based swaps on July 16, 2011;[21] and

- Provided temporary relief for entities providing certain clearing services for security-based swaps.[22]

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[20] *See* Release No. 34-64678, *Temporary Exemptions and Other Temporary Relief, Together with Information on Compliance Dates for New Provisions of the Securities Exchange Act of 1934 Applicable to Security-Based Swaps* (June 15, 2011), http://www.sec.gov/rules/exorders/2011/34-64678.pdf.

[21] *See* Release No. 34-64795, *Order Granting Temporary Exemptions under the Securities Exchange Act of 1934 in Connection with the Pending Revision of the Definition of "Security" to Encompass Security-Based Swaps, and Request for Comment* (July 1, 2011), http://sec.gov/rules/exorders/2011/34-64795.pdf; Release No. 33-9231, *Exemptions for Security-Based Swaps* (July 1, 2011), http://www.sec.gov/rules/interim/2011/33-9231.pdf; and Release No. 33-9383, *Extension of Exemptions for Security-Based Swaps* (January 29, 2013), http://www.sec.gov/rules/interim/2013/33-9383.pdf.

[22] *See* Release No. 34-64796, *Order Pursuant to Section 36 of the Securities Exchange Act of 1934 Granting Temporary Exemptions from Clearing Agency Registration Requirements under Section 17A(b) of the Exchange Act for Entities Providing Certain Clearing Services for Security-Based Swaps* (July 1, 2011), http://sec.gov/rules/exorders/2011/34-64796.pdf.

Next Steps for Implementation of Title VII: Application of Title VII in the Cross-Border Context

With very limited exceptions, the Commission has not addressed the application of the security-based swap provisions of Title VII in the cross-border context in its proposed or final rules. Rather than addressing these issues in a piecemeal fashion through each of the various substantive rulemakings implementing Title VII, we instead plan to address them holistically in a single proposing release. We believe this approach will provide investors, market participants, foreign regulators, and other interested parties with the opportunity to consider, as an integrated whole, the Commission's proposed approach to the application of the security-based swap provisions of Title VII in the cross-border context.

As we have indicated previously, we expect the scope of the effort to be broad. The proposal will address the application of Title VII in the cross-border context with respect to each of the major registration categories covered by Title VII for security-based swaps: security-based swap dealers; major security-based swap participants; security-based swap clearing agencies; security-based swap data repositories; and security-based swap execution facilities. It also will address the application of Title VII in connection with reporting and dissemination, clearing, and trade execution, as well as the sharing of information with regulators and related preservation of confidentiality with respect to data collected and maintained by security-based swap data repositories.

The cross-border release will involve notice-and-comment rulemaking, not just interpretive guidance. As a rulemaking proposal, the release will consider investor protection and incorporate an economic analysis that considers, among other things, the effects of the proposal on efficiency, competition, and capital formation. Although the rulemaking approach takes more time, we believe there are a number of benefits to this approach, including the opportunity to benefit from public input and the opportunity to provide a full articulation of the rationales for, and consideration of reasonable alternatives to, particular approaches that achieve the statutory purpose.

The Dodd-Frank Act specifically requires that the Commission, the CFTC, and the prudential regulators "consult and coordinate with foreign regulatory authorities on the establishment of consistent international standards" with respect to the regulation of OTC derivatives. The Commission has been actively working on a bilateral and multilateral basis with our fellow regulators abroad in such groups as the International Organization of Securities Commissions, the Financial Stability Board, and the OTC Derivatives Regulators Group, as we develop our proposed approach to cross-border issues under Title VII. Through these discussions and our participation in various international task forces and working groups, we also have gathered extensive information about foreign regulatory reform efforts, identified potential gaps, overlaps, and conflicts between U.S. and foreign regulatory regimes, and encouraged foreign regulators to develop rules and standards complementary to our own under the Dodd-Frank Act.

Additional Steps

In addition to proposing rules and interpretive guidance addressing the international implications of Title VII, the Commission expects to propose rules relating to books and records and reporting requirements for security-based swap dealers and major security-based swap participants. The Commission also expects soon to consider the application of mandatory clearing requirements to single-name credit default swaps, starting with those that were first cleared prior to the enactment of the Dodd-Frank Act.

Finally, the Commission staff continues to work diligently to develop recommendations for final rules required by Title VII that have been proposed but not yet been adopted, including rules relating to:

- Security-Based Swap Dealers and Major Security-Based Swap Participant Requirements;[23]
- Regulatory Reporting and Post-Trade Public Transparency;[24]
- Mandatory Clearing and Trade Execution and the Regulation of Clearing Agencies and Security-Based Swap Execution Facilities;[25] and
- Enforcement and Market Integrity.[26]

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[23] *See* Release No. 34-65543, *Registration of Security-Based Swap Dealers and Major Security-Based Swap Participants* (October 12, 2011), http://www.sec.gov/rules/proposed/2011/34-65543.pdf; 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), http://www.sec.gov/rules/proposed/2012/34-68071.pdf; Release No. 34-64766, *Business Conduct Standards for Security-Based Swaps Dealer and Major Security-Based Swap Participants* (June 29, 2011), http://www.sec.gov/rules/proposed/2011/34-64766.pdf; and Release No. 34-63727, *Trade Acknowledgment and Verification on Security-Based Swap Transactions* (January 14, 2011), http://www.sec.gov/rules/proposed/2011/34-63727.pdf.

[24] *See* Release No. 34-63346, *Regulation SBSR—Reporting and Dissemination of Security-Based Swap Information* (November 19, 2010), http://www.sec.gov/rules/proposed/2010/34-63346.pdf; and Release No. 34-63347, *Security-Based Swap Data Repository Registration, Duties, and Core Principles* (November 19, 2010), http://www.sec.gov/rules/proposed/2010/34-63347.pdf.

[25] *See* Release No. 34-63556, *End-User Exception of Mandatory Clearing of Security-Based Swaps* (December 15, 2010), http://www.sec.gov/rules/proposed/2010/34-63556.pdf; Release No. 34-63107, *Ownership Limitations and Governance Requirements for Security-Based Swap Clearing Agencies, Security-Based Swap Execution Facilities, and National Securities Exchanges with Respect to Security-Based Swaps under Regulation MC* (October 14, 2010), http://www.sec.gov/rules/proposed/2010/34-63107.pdf; and *Registration and Regulation of Security-Based Swap Execution Facilities* (February 2, 2011), http://www.sec.gov/rules/proposed/2011/34-63825.pdf.

[26] *See* Release No. 34-63236, *Prohibition Against Fraud, Manipulation, and Deception in Connection with Security-Based Swaps* (November 3, 2010), http://www.sec.gov/rules/proposed/2010/34-63236.pdf.

Clearing Agencies

Title VIII of the Dodd-Frank Act provides for increased regulation of financial market utilities[27] ("FMUs") and financial institutions that engage in payment, clearing, and settlement activities that are designated as systemically important. The purpose of Title VIII is to mitigate systemic risk in the financial system and promote financial stability. In addition, Title VII of the Dodd-Frank Act requires, among other things, that an entity acting as a clearing agency with respect to security-based swaps register with the Commission and that the Commission adopt rules with respect to clearing agencies that clear security-based swaps.

Adoption of Clearing Agency Standards

Clearing agencies play a critical role in the financial markets by ensuring that transactions settle on time and on agreed-upon terms. To promote the integrity of clearing agency operations and governance, the Commission adopted rules requiring all registered clearing agencies to maintain certain standards with respect to risk management and certain operational matters.[28] The rules also contain specific requirements for clearing agencies that perform central counterparty services. For example, such clearing agencies must have in place written policies and procedures reasonably designed to:

- Measure their credit exposures to participants at least once a day;

- Use margin requirements to limit their credit exposures to participants, to be reviewed at least monthly;

- Maintain sufficient financial resources to withstand, at a minimum, a default by the participant family to which the clearing agency has the largest exposure in extreme but plausible market conditions (with a higher requirement that agencies clearing security-based swaps maintain sufficient resources to cover the two largest participant family exposures); and

- Provide the opportunity to obtain membership in the clearing agency for persons who are not dealers or security-based swap dealers on fair and reasonable terms.

The rules also establish recordkeeping and financial disclosure requirements for all registered clearing agencies as well as several new standards for clearance and settlement.

The new rules were the result of close work between the Commission staff and staffs of the CFTC and the Board. The requirements take into consideration recognized international

[27] Section 803(6) of the Dodd-Frank Act defines a financial market utility as "any person that manages or operates a multilateral system for the purpose of transferring, clearing, or settling payments, securities, or other financial transactions among financial institutions or between financial institutions and the person."

[28] *See* Release No. 34-68080, *Clearing Agency Standards* (October 22, 2012), http://www.sec.gov/rules/final/2012/34-68080.pdf.

standards, and they are designed to further strengthen the Commission's oversight of securities clearing agencies, promote consistency in the regulation of clearing organizations generally, and thereby help to ensure that clearing agency regulation reduces systemic risk in the financial markets.

Systemically Important Clearing Agencies

SEC staff has worked with colleagues at the CFTC, the Board, the Department of Treasury, and other U.S. financial agencies on the designation of certain clearing agencies as systemically important FMUs. Title VIII of the Dodd-Frank Act provides important new enhancements to the regulation and supervision of designated FMUs that are designed to provide consistency, promote robust risk management and safety and soundness, reduce systemic risks, and support the stability of the broader financial system.[29]

Under Title VIII, FSOC is authorized to designate an FMU as systemically important if the failure or a disruption to the functioning of the FMU could create or increase the risk of significant liquidity or credit problems spreading among financial institutions or markets and thereby threaten the stability of the U.S. financial system. Since FSOC established an interagency FMU designations committee to develop a framework for the designation of systemically important FMUs, SEC staff has actively participated in the designations committee. In July 2012, FSOC designated six clearing agencies registered with the Commission as systemically important FMUs under Title VIII.[30] The SEC staff played an important role in preparing the analysis that provided the basis for these designations.

In addition, as directed by Title VIII and prior to the completion of the designation process, the SEC staff worked jointly with the staffs of the CFTC and the Board to develop a report to Congress containing recommendations regarding risk management supervision of clearing entities designated as systemically important. The staffs of the agencies met regularly to develop a framework for (1) improving consistency in the clearing entity oversight programs of the SEC and CFTC; (2) promoting robust risk management by designated clearing agencies; and (3) improving regulators' ability to monitor the potential effects of such risk management on the stability of the U.S. financial system. The joint report was submitted to Congress in July 2011.[31] Consistent with the framework set out in the report, the SEC has been engaged in ongoing consultation and cooperation in clearing agency oversight with the staffs of the CFTC and the Board.

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[29] *See* Dodd-Frank Act § 802.

[30] Clearing agencies that have been designated systemically important are Chicago Mercantile Exchange, Inc., The Depository Trust Company, Fixed Income Clearing Corporation, ICE Clear Credit LLC, National Securities Clearing Corporation, and The Options Clearing Corporation. Two payment systems were also designated systemically important: The Clearing House Payments Company L.L.C. on the basis of its role as operation of the Clearing House Interbank Payments System and CLS Bank International.

[31] *Risk Management Supervision of Designated Clearing Entities*, http://www.sec.gov/news/studies/2011/813study.pdf.

Staff Studies Regarding Investment Advisers and Broker-Dealers

In January 2011, the Commission submitted to Congress two staff studies in the investment management area required by the Dodd-Frank Act.

The first study, mandated by Section 914, analyzed the need for enhanced examination and enforcement resources for investment advisers registered with the Commission.[32] It found that the Commission likely will not have sufficient capacity in the near or long term to conduct effective examinations of registered investment advisers with adequate frequency. Therefore, the study stated that the Commission's examination program requires a source of funding adequate to permit the Commission to meet new examination challenges and sufficiently stable to prevent adviser examination resources from continuously being outstripped by growth in the number of registered investment advisers.

The study outlined the following three options for strengthening the Commission's investment adviser examination program: (1) imposing user fees on Commission-registered investment advisers to fund their examinations; (2) authorizing one or more self-regulatory organizations that assess fees on their members to examine, subject to Commission oversight, all Commission-registered investment advisers; or (3) authorizing FINRA to examine a subset of advisers – specifically, dually registered investment advisers and broker-dealers – for compliance with the Advisers Act.

The second staff study, required by Section 913 of the Dodd-Frank Act (the "IA/BD Study"), addressed the obligations of investment advisers and broker-dealers when providing personalized investment advice about securities to retail customers.[33] The staff study noted that retail investors generally are not aware of the differences between the regulation of investment advisers and broker-dealers, or the legal implications of those differences. The staff study also noted that many investors are confused by the different standards of care that apply to investment advisers and broker-dealers. The IA/BD Study made two primary recommendations: that the Commission (1) exercise the discretionary rulemaking authority provided by Section 913 of the Dodd-Frank Act to implement a uniform fiduciary standard of conduct for broker-dealers and investment advisers when they are providing personalized investment advice about securities to retail investors; and (2) consider harmonization of broker-dealer and investment adviser regulation when broker-dealers and investment advisers provide the same or substantially similar services to retail investors and when such harmonization adds meaningfully to investor protection.

[32] *See Study on Enhancing Investor Adviser Examinations* (January 2011), http://www.sec.gov/news/studies/2011/914studyfinal.pdf; *see also* Commissioner Elisse B. Walter, Statement on Study Enhancing Investment Adviser Examinations (Required by Section 914 of Title IX of the Dodd-Frank Wall Street Reform and Consumer Protection Act) (Jan. 2010), http://www.sec.gov/news/speech/2011/spch011911ebw.pdf.

[33] *See Study on Investment Advisers and Broker-Dealers* (January 2011), http://www.sec.gov/news/studies/2011/913studyfinal.pdf; *see also* Statement by SEC Commissioners Kathleen L. Casey and Troy A. Paredes Regarding Study on Investment Advisers and Broker-Dealers (January 21, 2011), http://www.sec.gov/news/speech/2011/spch012211klctap.htm.

Under Section 913, the uniform fiduciary standard to which broker-dealers and investment advisers would be subject would be "to act in the best interest of the customer without regard to the financial or other interest of the broker, dealer, or investment adviser providing the advice." The uniform fiduciary standard would be "no less stringent" than the standard that applies to investment advisers today.

We are giving serious consideration to the study's recommendations. Since publishing the IA/BD Study, the staff, including the Commission's economists, continues to review current information and available data about the marketplace for personalized investment advice and the potential impact of the study's recommendations. While we have extensive experience in the regulation of broker-dealers and investment advisers, we believe the public can provide further data and other information to assist us in determining whether or not to adopt a uniform fiduciary standard of conduct or otherwise use the authority provided under Section 913 of the Dodd-Frank Act. To this end, the staff is drafting a public request for information to obtain data specific to the provision of retail financial advice and the regulatory alternatives. The request aims to seek information from commenters – including retail investors, as well as industry participants – that will be helpful to us as we continue to analyze the various components of the market for retail financial advice.

Credit Rating Agencies

Under the Dodd-Frank Act, the Commission is required to undertake approximately a dozen rulemakings related to nationally recognized statistical rating organizations ("NRSROs"). The Act requires the SEC to address, among other things, internal controls and procedures, conflicts of interest, credit rating methodologies, transparency, ratings performance, analyst training, credit rating symbols and definitions, and disclosures accompanying the publication of credit ratings. The Commission adopted the first of these required rulemakings in January 2011,[34] and in May 2011 published for public comment a series of proposed rules that would further implement this requirement.[35] The proposed rules are intended to strengthen the integrity of credit ratings by, among other things, improving their transparency. Under the Commission's proposals, NRSROs would, among other things, be required to:

- Report on their internal controls;
- Better protect against conflicts of interest;

[34] *See* Release No. 33-9175, *Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act* (January 20, 2011), http://www.sec.gov/rules/final/2011/33-9175.pdf. In addition, in September 2010, the Commission issued an amendment to Regulation FD that implements Section 939B of the Act, which requires that the SEC amend Regulation FD to remove the specific exemption from the rule for disclosures made to NRSROs and credit rating agencies for the purpose of determining or monitoring credit ratings. *See* Release No. 33-9146, *Removal from Regulation FD of the Exemption for Credit Rating Agencies* (September 29, 2010), http://www.sec.gov/rules/final/2010/33-9146.pdf.

[35] *See* Release No. 34-64514, *Proposed Rules for Nationally Recognized Statistical Rating Organizations* (May 18, 2011), http://www.sec.gov/rules/proposed/2011/34-64514.pdf.

- Establish professional standards for their credit analysts;

- Provide, along with the publication of any credit rating, public disclosure about the credit rating and the methodology used to determine it; and

- Provide enhanced public disclosures about the performance of their credit ratings.

The Dodd-Frank Act also mandated three studies relating to credit rating agencies: (1) a study on the feasibility and desirability of standardizing credit rating terminology, which was published in September 2012;[36] (2) a study on alternative compensation models for rating structured finance products, which was published in December 2012;[37] and (3) a study on NRSRO independence, which the Commission staff is actively developing and which is due in July 2013.[38]

The Act also requires every federal agency to review its regulations that require use of credit ratings as an assessment of the credit-worthiness of a security and undertake rulemakings to remove these references and replace them with other standards of credit-worthiness deemed appropriate. In July 2011, the staff published a report discussing the following steps the Commission has taken to fulfill this requirement:[39]

- In July 2011, the Commission adopted rule amendments removing credit ratings as conditions for companies seeking to use short-form registration when registering non-convertible securities for public sale.[40] In addition, prior to adoption of the Act, in April 2010, the Commission proposed new requirements to replace the current credit rating references in shelf eligibility criteria for asset-backed security issuers with new shelf eligibility criteria.[41] In light of the Act and comment received on the April 2010 proposal, in July 2011, the Commission re-proposed the shelf eligibility criteria for offerings of asset-backed securities.

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[36] *Credit Rating Standardization Study* (September 2012), http://www.sec.gov/news/studies/2012/939h_credit_rating_standardization.pdf.

[37] *Report to Congress on Assigned Credit Ratings* (December 2012), http://www.sec.gov/news/studies/2012/assigned-credit-ratings-study.pdf. The staff is currently in the process of organizing a public roundtable to invite discussion from proponents and critics of the three courses of action discussed in the report.

[38] *See* Dodd-Frank Act § 939C.

[39] *Report on Review of Reliance on Credit Ratings* (July 2011), http://www.sec.gov/news/studies/2011/939astudy.pdf.

[40] *See* Release No. 33-9245, *Security Ratings* (July 27, 2011), http://www.sec.gov/rules/final/2011/33-9245.pdf.

[41] *See* Release No. 33-9117, *Asset-Backed Securities* (April 7, 2010), http://www.sec.gov/rules/proposed/2010/33-9117.pdf.

- In April 2011, the Commission proposed removing references to credit ratings in rules concerning broker-dealer financial responsibility, distributions of securities, and confirmations of transactions.[42] Also, in July 2012, the Commission issued an Interpretive Release in response to Section 939(e) of the Dodd-Frank Act, which removes references to credit ratings by NRSROs in two definitions in the Exchange Act.[43]

- In March 2011, the Commission proposed to remove credit ratings from rules relating to the types of securities in which a money market fund can invest and the treatment of repurchase agreements for certain purposes under the Investment Company Act as well as from the disclosure forms that certain investment companies must use.[44]

In September 2010, the Commission also adopted a rule amendment removing communications with credit rating agencies from the list of excepted communications in Regulation FD, as required by Section 939B of the Dodd-Frank Act.[45]

Finally, the Dodd-Frank Act requires the Commission to conduct staff examinations of each NRSRO at least annually and to issue an annual report summarizing the exam findings. As discussed in greater detail below, our staff recently completed the second cycle of these exams, and, following approval by the Commission, the staff's summary report of the examinations was published in November 2012.[46] The staff will continue to focus on completing the statutorily mandated annual examinations of each NRSRO, including follow-up from prior examinations, and making public the summary report of those examinations to promote compliance with statutory and Commission requirements. It also is taking steps in response to a recent International Organization of Securities Commissions preliminary recommendation to establish "colleges" of regulators to provide a framework for information exchange and collaboration with foreign counterparts regarding large globally active credit rating agencies.[47]

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[42] *See* Release No. 34-64352, *Removal of Certain References to Credit Ratings under the Securities Exchange Act of 1934* (April 27, 2011), http://www.sec.gov/rules/proposed/2011/34-64352.pdf.

[43] *See* Release No. 34-67448, *Commission Guidance Regarding Definitions of Mortgage Related Security and Small Business Related Security* (July 17, 2012), http://www.sec.gov/rules/interp/2012/34-67448.pdf.

[44] *See* Release Nos. 33-9193; IC-29592, *References to Credit Ratings in Certain Investment Company Act Rules and Forms* (March 3, 2011), http://www.sec.gov/rules/proposed/2011/33-9193.pdf. In addition, in November 2012, the Commission adopted a rule establishing a credit quality standard that certain investments by business and industrial development companies must satisfy for those companies to qualify for an exemption from most provisions of the Investment Company Act. *Purchase of Certain Debt Securities by Business and Industrial Development Companies Relying on an Investment Company Act Exception* (November 19, 2012), http://www.sec.gov/rules/final/2012/ic-30268.pdf.

[45] *See* Release No. 33-9146, *Removal from Regulation FD of the Exemption for Credit Rating Agencies* (September 29, 2010), http://www.sec.gov/rules/final/2010/33-9146.pdf.

[46] *2012 Summary Report of Commission Staff's Examinations of Each Nationally Recognized Statistical Rating Organization* (November 2012), http://www.sec.gov/news/studies/2012/nrsro-summary-report-2012.pdf.

[47] *See* Release No. IOSCO/MR/34/2012, *IOSCO Publishes Two Reports Advancing its Work on Credit Rating Agencies* (Dec. 21, 2012) http://www.iosco.org/news/pdf/IOSCONEWS261.pdf.

Volcker Rule

In October 2011, the Commission proposed a rule jointly with the Board, the Federal Deposit Insurance Corporation, and the Office of the Comptroller of the Currency (collectively, the "Federal banking agencies") to implement Section 619 of the Dodd-Frank Act, commonly referred to as the "Volcker Rule."[48] This proposal reflects an extensive, collaborative effort among the Federal banking agencies, the SEC, and the CFTC, under the coordination of the Department of the Treasury ("Treasury"), to design a rule to implement the Volcker Rule's prohibitions and restrictions in a manner that is consistent with the language and purpose of the statute.[49]

As required by Section 619, the joint proposal generally prohibits banking entities — including bank-affiliated, SEC-registered broker-dealers, security-based swap dealers, and investment advisers—from engaging in proprietary trading and having certain interests in, and relationships with, hedge funds and private equity funds ("covered funds")[50]. Like the statute, the proposed rule provides certain exceptions to these general prohibitions. For example, the proposal permits a banking entity to engage in underwriting, market making-related activity, risk-mitigating hedging, and organizing and offering a covered fund, among other permitted activities, provided that specific requirements are met. Further, consistent with the statute, an otherwise-permitted activity would be prohibited if it involved a material conflict of interest, high-risk assets or trading strategies, or a threat to the safety and soundness of the banking entity or to the financial stability of the United States. As set forth in the Dodd-Frank Act, the Commission's rule would apply to banking entities for which the Commission is the primary financial regulatory agency, including, among others, certain SEC-registered broker-dealers, investment advisers, and security-based swap dealers.

The joint proposal sought comment on a wide range of topics due, in part, to the breadth of issues presented by the statute and the proposal. In response, the Commission has received nearly 19,000 comment letters, including more than 600 unique and detailed letters.[51] These

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[48] *See* Release No. 34-65545, *Prohibitions and Restrictions on Proprietary Trading and Certain Interests in, and Relationships With, Hedge Funds and Private Equity Funds* (October 12, 2011), http://www.sec.gov/rules/proposed/2011/34-65545.pdf. The CFTC issued a substantially similar proposal in January 2012, which was published in the Federal Register in February 2012. *See* 77 FR 8332 (February 14, 2012), http://www.cftc.gov/LawRegulation/FederalRegister/ProposedRules/2012-935.

[49] In developing this proposal, interagency staffs gave close and thoughtful consideration to the FSOC's January 2011 study and its recommendations for implementing Section 619, which can be found at http://www.treasury.gov/initiatives/Documents/Volcker%20sec%20%20619%20study%20final%201%2018%2011%20rg.pdf. As a result, the joint proposal builds upon many of the recommendations set forth in the FSOC study.

[50] Section 619 defines "banking entity" as any insured depository institution (other than certain limited purpose trust institutions), any company that controls an insured depository institution, any company that is treated as a bank holding company for purposes of section 8 of the International Banking Act of 1978 (*i.e.*, a foreign entity with a branch, agency, or subsidiary bank operation in the U.S.), and any affiliate or subsidiary of any of the foregoing entities. *See* 12 U.S.C. 1851(h)(1).

[51] The Commission and the Federal banking agencies extended the comment period for the joint proposal from January 13, 2012 to February 13, 2012. *See* Release No. 34-66057 (December 23, 2011),

comments represent a wide variety of viewpoints on a number of complex topics, and we are closely considering them as we continue to work with the Federal banking agencies, the CFTC, and Treasury to develop rules to implement Section 619. Staffs from each of the regulatory agencies and Treasury are engaged in regular and active consultation to determine how best to move forward to implement the statute.

Pursuant to the Dodd-Frank Act, the statutory requirements of Section 619 became effective on July 21, 2012. However, the statute also provides for a conformance period following the effective date. Section 619 authorizes the Board to establish rules regarding the conformance period. The Board issued a conformance rule in February 2011[52] and a related policy statement in April 2012, which confirmed that banking entities have two years, beginning July 21, 2012, to conform all of their activities and investments to the requirements of Section 619, unless the Board extends the conformance period.[53]

Municipal Advisors

Section 975 of the Dodd-Frank Act creates a new class of regulated persons, "municipal advisors," and requires these advisors to register with the Commission. This new registration requirement, which became effective on October 1, 2010, makes it unlawful for any municipal advisor, among other things, to provide advice to a municipal entity unless the advisor is registered with the Commission. In September 2010, the Commission adopted, and subsequently extended, an interim final rule establishing a temporary means for municipal advisors to satisfy the registration requirement.[54] The Commission has received over 1,100 confirmed registrations of municipal advisors pursuant to this temporary rule.

In December 2010, the Commission proposed a permanent rule to govern municipal advisor registration with the SEC.[55] We have received over 1,000 comment letters on the proposal. Many expressed concern that the proposed rules were overbroad in various respects, including their potential impact on appointed board members of municipal entities, municipal investments unrelated to municipal securities, and traditional banking products and services.

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http://www.sec.gov/rules/proposed/2011/34-66057.pdf. The Commission's public comment file is available at http://www.sec.gov/comments/s7-41-11/s74111.shtml.

[52] *See* 76 FR 8265 (February 14, 2011).

[53] *See* 77 FR 33949 (June 8, 2012). The Board policy statement further provides that, during the conformance period, banking entities should engage in good-faith planning efforts, appropriate for their activities and investments, to enable them to conform their activities and investments to the requirements of Section 619 and final implementing rules by no later than the end of the conformance period.

[54] *See* Release No. 34-62824, *Temporary Registration of Municipal Advisors* (September 1, 2010), http://www.sec.gov/rules/interim/2010/34-62824.pdf.

[55] *See* Release No. 34-63576, *Registration of Municipal Advisors* (December 20, 2010), http://sec.gov/rules/proposed/2010/34-63576.pdf.

Finalizing the permanent rules for the registration of municipal advisors is now the highest immediate priority of the SEC's newly established Office of Municipal Securities.[56] We anticipate that the final rules would address, among other things, the well-publicized concerns about the need for an exception from registration for appointed board members of municipal entities. In addition, the staff is continuing to discuss many interpretive issues with other regulators and interested market participants in pursuit of a final rule that requires appropriate registration of parties engaging in municipal advisory activities without unnecessarily imposing additional regulation.

Asset-Backed Securities

The Commission has been active in implementing Subtitle D of Title IX of the Dodd-Frank Act, entitled "Improvements to the Asset-Backed Securitization Process." In August 2011**,** the Commission adopted rules in connection with Section 942(a) of the Act, which eliminated the automatic suspension of the duty to file reports under Section 15(d) of the Exchange Act for asset-backed security ("ABS") issuers and granted the Commission authority to issue rules providing for the suspension or termination of this duty to file reports. The new rules permit suspension of the reporting obligations for ABS issuers when there are no longer asset-backed securities of the class sold in a registered transaction held by non-affiliates of the depositor.[57]

The Commission also is working closely with other regulators to jointly create the risk retention rules required by Section 941 of the Act, which will address the appropriate amount, form and duration of required risk retention for ABS securitizers and will define qualified residential mortgages ("QRMs"). On March 30, 2011, the Commission joined its fellow regulators in issuing for public comment proposed risk retention rules to implement Section 941.[58]

Under the proposed rules, a sponsor generally would be permitted to choose from a menu of four risk retention options to satisfy its minimum five percent risk retention requirement. These options were designed to provide sponsors with flexibility while also ensuring that they actually retain credit risk to align incentives. The proposed rules also include three transaction-

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[56] The Office of Municipal Securities is described in more detail below.

[57] *See* Release No. 34-65148, *Suspension of the Duty to File Reports for Classes of Asset-Backed Securities under Section 15(d) of the Securities Exchange Act of 1934* (August 17, 2011), http://www.sec.gov/rules/final/2011/34-65148.pdf.

[58] *See* Release No. 34-64148, *Credit Risk Retention* (March 30, 2011), http://www.sec.gov/rules/proposed/2011/34-64148.pdf. Section 941, is codified as the new Section 15G of the Exchange Act. It generally requires the Commission, the Board, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency and, in the case of the securitization of any "residential mortgage asset," the Federal Housing Finance Agency and Department of Housing and Urban Development, to jointly prescribe regulations that require a securitizer to retain not less than five percent of the credit risk of any asset that the securitizer, through the issuance of an asset-backed security, transfers, sells, or conveys to a third party. Section 15G also provides that the jointly-prescribed regulations must prohibit a securitizer from directly or indirectly hedging or otherwise transferring the credit risk that the securitizer is required to retain. *See* § 78o-11(c)(1)(A).

specific options related to securitizations involving revolving asset master trusts, asset-backed commercial paper conduits, and commercial mortgage-backed securities. Also, as required by Section 941, the proposal provides a complete exemption from the risk retention requirements for ABS collateralized solely by QRMs and establishes the terms and conditions under which a residential mortgage would qualify as a QRM. We have received a number of comments regarding the QRM exemption, as well as concerning other aspects of the proposal.[59] The staff currently is considering those comments and diligently working with the other agencies' staff to move forward with this interagency rulemaking.

In January 2011 the Commission also adopted rules on the use of representations and warranties in the market for ABS as required by the Act's Section 943.[60] The rules required ABS issuers to disclose the history of repurchase requests received and repurchases made relating to their outstanding ABS. Issuers were required to make their initial filing on February 14, 2012, disclosing the repurchase history for the three years ending December 31, 2011. The disclosure requirements apply to issuers of registered and unregistered ABS, including municipal ABS, though the rules provide municipal ABS an additional three-year phase-in period.

The Commission also adopted rules in January 2011 to implement Section 945, which required an asset-backed issuer in a Securities Act registered transaction to perform a review of the assets underlying the ABS and disclose the nature of such review.[61] Under the final rules, the type of review conducted may vary, but at a minimum must be designed and effected to provide reasonable assurance that the prospectus disclosure about the assets is accurate in all material respects. The final rule provided a phase-in period to allow market participants to adjust their practices to comply with the new requirements.

Prohibition against Conflicts of Interest in Certain Securitizations

In September 2011, the Commission proposed a rule to implement the prohibition under Section 621 of the Act, which prohibited entities that create and distribute ABS from engaging in transactions that involve or result in material conflicts of interest with respect to the investors in such ABS.[62] The proposed rule would implement this provision by prohibiting underwriters, placement agents, initial purchasers, sponsors of ABS, or any affiliate or subsidiary of such entity from engaging in any transaction that would involve or result in any material conflicts of interest with respect to any investor in the relevant ABS. These entities, referred to as "securitization participants," assemble, package, and distribute ABS, so they may benefit from

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[59] The SEC received letters on the proposal from over 10,000 commentators, representing approximately 275 unique comment letters.

[60] *See* Release No. 33-9175, *Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act* (January 20, 2011), http://www.sec.gov/rules/final/2011/33-9175.pdf.

[61] *See* Release No. 33-9176, *Issuer Review of Assets in Offerings of Asset-Backed Securities* (January 20, 2011), http://www.sec.gov/rules/final/2011/33-9176.pdf.

[62] *See* Release No. 34-65355, *Prohibition against Conflicts of Interest in Certain Securitizations* (September 19, 2011), http://www.sec.gov/rules/proposed/2011/34-65355.pdf.

the activity that Section 621 is designed to prohibit. The prohibition would apply to both non-synthetic and synthetic asset-backed securities and would apply to both registered and unregistered offerings of asset-backed securities.

The proposal is not intended to prohibit legitimate securitization activities. We asked many questions in the release to help us strike the right balance of prohibiting the type of conduct at which the statute is targeted without restricting legitimate securitization activities. The Commission received a number of comments on the proposal, and the staff is carefully considering those comments in preparing its recommendation to the Commission.

Corporate Governance and Executive Compensation

The Dodd-Frank Act includes a number of corporate governance and executive compensation provisions that require Commission rulemaking. Among others, such rulemakings include:

- **Say on Pay.** In accordance with Section 951 of the Act, in January 2011 the Commission adopted rules that require public companies subject to the federal proxy rules to provide a shareholder advisory "say-on-pay" vote on executive compensation, a separate shareholder advisory vote on the frequency of the say-on-pay vote, and disclosure about, and a shareholder advisory vote to approve, compensation related to merger or similar transactions, known as "golden parachute" arrangements.[63] Companies (other than smaller reporting companies) began providing these say-on-pay and "say-on-frequency" advisory votes at shareholder meetings occurring on or after January 21, 2011. The rules provided smaller reporting companies a two-year delayed compliance period for the say-on-pay and "frequency" votes, and those companies began complying with the rules on January 21, 2013. The Commission also proposed rules to implement the Section 951 requirement that institutional investment managers report their votes on these matters at least annually.[64]

- **Compensation Committee and Adviser Requirements.** In June 2012, the Commission adopted rules to implement Section 952 of the Act, which requires the Commission to, by rule, direct the national securities exchanges and national securities associations to prohibit the listing of any equity security of an issuer that does not comply with new compensation committee and compensation adviser requirements.[65] The new rules direct the exchanges to establish listing standards concerning compensation advisers and listing standards that require each member of a listed issuer's compensation committee to be an "independent" member of the board of directors. The rules also require disclosure about

[63] *See* Release No. 33-9178, *Shareholder Approval of Executive Compensation and Golden Parachute Compensation* (January 25, 2011), http://www.sec.gov/rules/final/2011/33-9178.pdf.

[64] *See* Release No. 34-63123, *Reporting of Proxy Votes on Executive Compensation and Other Matters* (October 18, 2010), http://www.sec.gov/rules/proposed/2010/34-63123.pdf.

[65] *See* Release No. 33-9330, *Listing Standards for Compensation Committees* (June 20, 2012), http://www.sec.gov/rules/final/2012/33-9330.pdf.

the use of compensation consultants and related conflicts of interest. Each national securities exchange must have final rules or rule amendments complying with the new rules approved by the Commission no later than June 27, 2013. To conform their rules governing independent compensation committees to the new requirements, national securities exchanges that have rules providing for the listing of equity securities have filed proposed rule changes with the Commission.[66] The Commission issued final orders approving the proposed rule changes in January 2013.[67]

- **Incentive-Based Compensation Arrangements**. Section 956 of the Dodd-Frank Act requires the Commission, along with six other financial regulators, to jointly adopt regulations or guidelines governing the incentive-based compensation arrangements of certain financial institutions, including broker-dealers and investment advisers with $1 billion or more of assets. Working with the other regulators, in March 2011 the Commission published for public comment a proposed rule that would address such arrangements.[68] The Commission has received many comment letters on the proposed rule, and the Commission staff, together with staff from the other regulators, is carefully considering the issues and concerns raised in those comments before adopting final rules.

- **Prohibition on Broker Voting of Uninstructed Shares**. Section 957 of the Act requires the rules of each national securities exchange to be amended to prohibit brokers from voting uninstructed shares in director elections (other than uncontested elections of directors of registered investment companies), executive compensation matters, or any other significant matter, as determined by the Commission by rule. The Commission has

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[66] *See* Release No. 34-68022 (October 9, 2012), http://www.sec.gov/rules/sro/bats/2012/34-68022.pdf (BATS Exchange, Inc.); Release No. 34-68020 (October 9, 2012), http://www.sec.gov/rules/sro/cboe/2012/34-68020.pdf (Chicago Board of Options Exchange, Inc.); Release No. 34-68033 (October 10, 2012), http://www.sec.gov/rules/sro/chx/2012/34-68033.pdf (Chicago Stock Exchange, Inc.); Release No. 34-68013 (October 9, 2012), http://www.sec.gov/rules/sro/nasdaq/2012/34-68013.pdf (Nasdaq Stock Market LLC); Release No. 34-68018 (October 9, 2012), http://www.sec.gov/rules/sro/bx/2012/34-68018.pdf (Nasdaq OMX BX, Inc.); Release No. 34-68039 (October 11, 2012), http://www.sec.gov/rules/sro/nsx/2012/34-68039.pdf (National Stock Exchange, Inc.); Release No. 34-68011 (October 9, 2012), http://www.sec.gov/rules/sro/nyse/2012/34-68011.pdf (New York Stock Exchange LLC); Release No. 34-68006 (October 9, 2012), http://www.sec.gov/rules/sro/nysearca/2012/34-68006.pdf (NYSEArca LLC); Release No. 34-68007 (October 9, 2012), http://www.sec.gov/rules/sro/nysemkt/2012/34-68007.pdf (NYSE MKT LLC).

[67] *See* Release No. 34-68643 (January 11, 2013), http://www.sec.gov/rules/sro/bats/2013/34-68643.pdf (BATS Exchange, Inc.); Release No. 34-68642 (January 11, 2013), http://www.sec.gov/rules/sro/cboe/2013/34-68642.pdf (Chicago Board of Options Exchange, Inc.); Release No. 34-68653 (January 14, 2013), http://www.sec.gov/rules/sro/chx/2013/34-68653.pdf (Chicago Stock Exchange, Inc.); Release No. 34-68640 (January 11, 2013), http://www.sec.gov/rules/sro/nasdaq/2013/34-68640.pdf (Nasdaq Stock Market LLC); Release No. 34-68641 (January 11, 2012), http://www.sec.gov/rules/sro/bx/2013/34-68641.pdf (Nasdaq OMX BX, Inc.); Release No. 34-68662 (January 15, 2012), http://www.sec.gov/rules/sro/nsx/2013/34-68662.pdf (National Stock Exchange, Inc.); Release No. 34-68635 (January 11, 2013), http://www.sec.gov/rules/sro/nyse/2013/34-68635.pdf (New York Stock Exchange LLC); Release No. 34-68638 (January 11, 2013), http://www.sec.gov/rules/sro/nysearca/2013/34-68638.pdf (NYSEArca LLC); Release No. 34-68637 (January 11, 2013), http://www.sec.gov/rules/sro/nysemkt/2013/34-68637.pdf (NYSE MKT LLC).

[68] *See* Release no. 34-64140 (March 29, 2011), http://www.sec.gov/rules/proposed/2011/34-64140.pdf.

approved changes to the rules with regard to director elections and executive compensation matters for all of the national securities exchanges.[69]

The Commission also is required by the Act to adopt several additional rules related to corporate governance and executive compensation, including rules mandating new listing standards relating to specified "clawback" policies[70] and new disclosure requirements about executive compensation and company performance,[71] executive pay ratios,[72] and employee and director hedging.[73] The staff is working diligently on developing recommendations for the Commission concerning the implementation of these provisions of the Act.

Specialized Disclosure Provisions

Title XV of the Act contains specialized disclosure provisions related to conflict minerals, coal or other mine safety, and payments by resource extraction issuers to foreign or U.S. government entities. The Commission adopted final rules for the mine safety provision in December 2011,[74] and companies are currently complying with those rules. In addition, the Commission adopted final rules for disclosure relating to conflict minerals and payments by

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[69] *See* Release No. 34-62874 (September 9, 2010), http://www.sec.gov/rules/sro/nyse/2010/34-62874.pdf (New York Stock Exchange); Release No. 34-62992 (September 24, 2010), http://www.sec.gov/rules/sro/nasdaq/2010/34-62992.pdf (NASDAQ Stock Market LLC); Release No. 34-63139 (October 20, 2010), http://www.sec.gov/rules/sro/ise/2010/34-63139.pdf (International Securities Exchange); Release No. 34-63917 (February 16, 2011), http://www.sec.gov/rules/sro/cboe/2011/34-63917.pdf (Chicago Board Options Exchange); Release No. 34-63918 (February 16, 2011), http://www.sec.gov/rules/sro/c2/2011/34-63918.pdf (C2 Options Exchange, Incorporated); Release No. 34-64023 (March 3, 2011), http://www.sec.gov/rules/sro/bx/2011/34-64023.pdf (NASDAQ OMX BX, Inc.); Release No. 34-64024 (March 3, 2011), http://www.sec.gov/rules/sro/bx/2011/34-64024.pdf (Boston Options Exchange Group, LLC); Release No. 34-64121 (March 24, 2011), http://www.sec.gov/rules/sro/chx/2011/34-64121.pdf (Chicago Stock Exchange); Release No. 34-64122 (March 24, 2011), http://www.sec.gov/rules/sro/phlx/2011/34-64122.pdf (NASDAQ OMX PHLX LLC); Release No. 34-64186 (April 5, 2011), http://www.sec.gov/rules/sro/edgx/2011/34-64186.pdf (EDGX Exchange); Release No. 34-64187 (April 5, 2011), http://www.sec.gov/rules/sro/edga/2011/34-64187.pdf (EDGA Exchange); Release No. 34-65449 (September 30, 2011), http://www.sec.gov/rules/sro/bats/2011/34-65449.pdf (BATS Exchange, Inc.); Release No. 34-65448 (September 30, 2011), http://www.sec.gov/rules/sro/byx/2011/34-65448.pdf (BATS Y-Exchange, Inc.); Release No. 34-65804 (November 22, 2011), http://www.sec.gov/rules/sro/nsx/2011/34-65804.pdf (National Stock Exchange, Inc.); Release No. 34-66006 (December 20, 2011) http://www.sec.gov/rules/sro/nyseamex/2011/34-66006.pdf. (NYSE Amex LLC); Release No. 34-66192 (January 19, 2012), http://www.sec.gov/rules/sro/nysearca/2012/34-66192.pdf (NYSE Arca, Inc.); and Release No. 68723 (January 24, 2013) (MIAX-2013-02).

[70] *See* Section 954 of the Dodd-Frank Act.

[71] *See* Section 953(a) of the Dodd-Frank Act.

[72] *See* Section 953(b) of the Dodd-Frank Act.

[73] *See* Section 955 of the Dodd-Frank Act.

[74] *See* Release No. 33-9286, Mine Safety Disclosure, (December 21, 2011), http://www.sec.gov/rules/final/2011/33-9286.pdf.

resource extraction issuers in August 2012.[75] The conflict minerals and resource extraction issuer rulemakings were effective in November 2012 and established phase-in periods for compliance to provide issuers time to establish systems and processes to comply with the new rules. Companies subject to the conflict minerals disclosure requirement will be required to make their first filing with the disclosure on new Form SD on May 31, 2014 for the 2013 calendar year. Companies subject to the resource extraction issuer disclosure requirement will be required to comply with the rules for fiscal years ending after September 30, 2013. The conflict minerals and resource extraction issuer rulemakings are subject to pending litigation.[76]

Exempt Offerings

In December 2011, the Commission adopted rule amendments to implement Section 413(a) of the Act, which requires the Commission to exclude the value of an individual's primary residence when determining if that individual's net worth exceeds the $1 million threshold required for "accredited investor" status.[77] Section 413(a) was effective on the date of enactment of the Dodd-Frank Act and the implementing rules clarify the requirements and codify them in the Commission's rules.

Under Section 926 of the Act, the Commission is required to adopt rules that disqualify securities offerings involving certain "felons and other 'bad actors'" from relying on the safe harbor from Securities Act registration provided by Rule 506 of Regulation D. The Commission proposed rules to implement the requirements of Section 926 on May 25, 2011.[78] Under the proposal, the disqualifying events include certain criminal convictions, court injunctions and restraining orders; certain final orders of state securities, insurance, banking, savings association or credit union regulators, federal banking agencies or the National Credit Union Administration; certain types of Commission disciplinary orders; suspension or expulsion from membership in, or from association with a member of, a securities self-regulatory organization; and certain other securities-law related sanctions. The comment period for this rule proposal has ended and the staff is developing recommendations for final rules.

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[75] *See* Release No. 34-67716, *Conflict Minerals* (August 22, 2012), http://www.sec.gov/rules/final/2012/34-67716.pdf and *Disclosure of Payments by Resource Extraction Issuers* (August 22, 2012), http://www.sec.gov/rules/final/2012/34-67717.pdf.

[76] *See* American Petroleum Institute, et al. v. United States Securities and Exchange Commission, No. 12-1398 (D.C. Cir. filed Oct. 10, 2012) and National Association of Manufacturers, et al. v. United States Securities and Exchange Commission, No. 12-1422 (D.C. Cir. filed Oct. 19, 2012). The Commission received a motion requesting that it stay the newly-adopted disclosure rules for resource extraction issuers, but the Commission declined to issue a stay order. *See* http://www.sec.gov/rules/final/2012/34-67717-motion-stay.pdf and Release No. 68197 (November 8, 2012), http://www.sec.gov/rules/other/2012/34-68197.pdf. The petitioners in the litigation concerning the conflict minerals rule did not request a stay of the newly-adopted rule.

[77] *See* Release No. 33-9287, *Net Worth Standard for Accredited Investors* (December 21, 2011) and (March23, 2012), http://www.sec.gov/rules/final/2011/33-9287.pdf and http://www.sec.gov/rules/final/2012/33-9287a.pdf (technical amendment).

[78] *See* Release No. 33-9211, *Disqualification of Felons and Other "Bad Actors" from Rule 506 Offerings* (May 25, 2011), http://www.sec.gov/rules/proposed/2011/33-9211.pdf.

Financial Stability Oversight Council

Title I of the Dodd-Frank Act provides that the Chairman of the SEC shall serve as a voting member of FSOC. FSOC provides a formal structure for coordination among the various financial regulators to monitor systemic risk and to promote financial stability across our nation's financial system. As Chairman of the SEC, I participate in the systemic risk oversight activities of the Council and coordinate with my colleagues on the Council to facilitate efficient and effective implementation of the Dodd-Frank Act.

New Commission Offices

In addition to the Office of the Whistleblower mentioned above, the Dodd-Frank Act required the Commission to create four new offices: the Office of Credit Ratings, Office of the Investor Advocate, Office of Minority and Women Inclusion, and Office of Municipal Securities. As each of these offices is statutorily required to report directly to the Chairman, the creation of these offices was subject to approval by the Commission's Appropriations subcommittees.

Office of Credit Ratings

As required by Section 932, the Commission established an Office of Credit Ratings ("OCR") with the appointment of OCR's Director in June 2012. OCR is charged with administering the rules of the Commission with respect to the practices of NRSROs in determining credit ratings for the protection of users of credit ratings and in the public interest, promoting accuracy in credit ratings issued by NRSROs and ensuring that credit ratings are not unduly influenced by conflicts of interest and that NRSROs provide greater disclosure to investors. OCR conducts examinations of NRSROs to assess and promote compliance with statutory and Commission requirements, monitors the activities of NRSROs, and provides guidance with respect to the Commission's policy and regulatory initiatives related to NRSROs.

The examination activities of OCR are focused on conducting annual, risk-based examinations of all registered NRSROs to assess compliance with federal securities laws and Commission rules. OCR also conducts special risk-targeted examinations based on credit market issues and concerns and to follow up on tips, complaints, and NRSRO self-reported incidents. The monitoring activities of OCR are geared towards informing Commission policy and rulemaking and include identifying and analyzing risks, monitoring industry trends, and administering and monitoring the NRSRO registration process as well as the periodic updates by existing registrants of their Forms NRSRO.

The Dodd-Frank Act requires that the SEC conduct examinations of each NRSRO at least annually. OCR's scope for NRSRO examinations includes covering all eight areas required by the Dodd-Frank Act. Beginning in 2012, in an effort to be more tailored, OCR developed a risk-based approach to exam planning, identifying different risks for different NRSROs. During examinations, OCR also follows up on findings from prior exams and areas of identified risks. OCR prepares an annual public examination report as required by the Dodd-Frank Act, which summarizes the essential findings of the examinations and provides information on whether the

NRSROs have appropriately addressed any previous examination recommendations. In November 2012, staff issued the second annual staff report including those findings.[79]

Office of the Investor Advocate

Section 915 requires the SEC to establish an Office of the Investor Advocate to assist retail investors in resolving significant problems they may have with the Commission or with SROs. The Investor Advocate also will identify areas in which investors would benefit from changes in Commission regulations or SRO rules; identify problems that investors have with financial service providers and investment products; and analyze the potential impact on investors of proposed Commission regulations and SRO rules. The Investor Advocate also must hire an Ombudsman, whose activities will be included in the Advocate's reports to Congress. The Commission is in the process of filling the position of Investor Advocate.

Office of Minority and Women Inclusion

In July 2011, shortly after the House and Senate Appropriations Committees approved the SEC's reprogramming request to create the office, the SEC formally established its Office of Minority and Women Inclusion ("OMWI"). The OMWI Director joined the office in January 2012.

Under a broad outreach strategy developed by OMWI, the SEC has sponsored and/or attended more than 40 career fairs, conferences, and business matchmaking events to market the SEC to diverse suppliers and jobseekers. OMWI continues to partner with leading organizations focused on developing employment opportunities for minorities and women at the SEC and in the financial services industry. In addition, the OMWI Director, along with OMWI directors from other agencies, participated in joint roundtables with financial industry groups and trade organizations to foster informed dialogue regarding the development of standards for assessing the diversity policies and practices of regulated entities.

In fiscal year 2012, OMWI provided technical assistance to over 150 vendors in its efforts to expand contracting opportunities for minority-owned and women-owned businesses. While we are pleased that the percentage of contracting dollars awarded to minority-owned and women-owned businesses – as well as the percentages of minority hires for certain demographic groups, including African-Americans – increased from fiscal year 2011, more needs to be done. OMWI and the Commission are committed to continuing to work proactively to encourage diversity in the workforce and increase the participation of minority-owned and women-owned businesses in the SEC's programs and contracting opportunities.

Office of Municipal Securities

Section 979 of the Dodd-Frank Act required the Commission to establish an Office of Municipal Securities ("OMS"), reporting directly to the Chairman, to administer the rules pertaining to broker-dealers, advisors, investors and issuers of municipal securities, and to

[79] *See SEC Issues Staff Summary Report of Examinations of Nationally Recognized Statistical Rating Organizations,* 2012-228 (November 2012), http://www.sec.gov/news/studies/2012/nrsro-summary-report-2012.pdf.

coordinate with the MSRB on rulemaking and enforcement actions. In August 2012, the Commission announced the establishment of the OMS and appointed a director. The office was previously part of the Division of Trading and Markets. One purpose behind this legislative mandate was to focus priority attention on the significant municipal securities market, which encompasses over $3.7 trillion in outstanding municipal securities, over 44,000 municipal issuers, and an average of over 12,000 bond issues annually.

The highest immediate priority project for OMS is to work together with the Division of Trading and Markets to finalize pending rules regarding registration of municipal advisors. OMS's current initiatives also include assisting with the implementation of disclosure and market structure initiatives recommended for potential further consideration by the Commission in its Report on the Municipal Securities Market, issued on July 31, 2012, following a staff review of this market sector. Briefly, these recommended initiatives include:

- a series of legislative recommendations for potential further consideration to grant the Commission direct authority to set baseline disclosure and accounting standards for municipal issuers;

- regulatory disclosure recommendations for potential further consideration to update the Commission's 1994 interpretative release concerning the disclosure obligations of issuers of municipal securities; and

- a series of market structure recommendations for potential further consideration to improve price transparency in the municipal securities market.

As noted in this Report, further action on specific recommendations will involve further study of relevant additional information, including information, as applicable, related to the costs and benefits of the recommendations and the consideration, as applicable, of public comment.

Economic Analysis

The SEC considers economic analysis to be a critical element of its rulewriting process. We are mindful that our rules have both costs and benefits, and that the steps we take to protect the investing public also impact financial markets and industry participants who must comply with our rules. In recent years, even in the face of an unprecedented rulemaking burden generated by the passage of the Act, the agency has continually enhanced its economic analysis efforts by, among other things, hiring additional Ph.D. economists and involving our economists earlier and more comprehensively in the rulemaking process. In addition, last year SEC staff received new guidance to inform the manner in which they incorporate economic analysis into their rulemaking work.[80]

Our Division of Risk, Strategy, and Financial Innovation ("RSFI") directly assists in the rulemaking process by helping develop the conceptual framing for, and assisting in the

[80] The memorandum "Current Guidance on Economic Analysis in SEC Rulemakings" is available at http://www.sec.gov/divisions/riskfin/rsfi_guidance_econ_analy_secrulemaking.pdf. The guidance is in effect and being followed by the rule writing teams as they develop rule recommendations.

subsequent writing of, the economic analysis in rule releases. Economic analysis of agency rules considers, among other things, the direct and indirect costs and benefits of the Commission's proposed regulations and reasonable alternative approaches, and the rule's effects on competition, efficiency and capital formation. Of course, analysis of the likely economic effects of proposed rules, while critical to the rulemaking process, can be challenging, and certain costs or benefits may be difficult to quantify or value with precision, particularly those that are indirect or intangible. We continue to be committed to meeting these challenges and to ensuring that the Commission engages in sound, robust analysis in its rulemaking, and we will continue to work to enhance both the process and substance of that analysis.

Section 967 Organizational Assessment

Section 967 of the Act directed the agency to engage the services of an independent consultant to study a number of specific SEC internal operations. Boston Consulting Group, Inc. ("BCG") performed the assessment and provided recommended initiatives in March 2011.[81] The recommendations targeted various aspects of the SEC's mission, function, structure, and operations, including:

- restructuring operating divisions and support offices;
- reshaping roles and governance;
- assessing potential reprioritization of regulatory activities;
- reviewing Commission-staff interaction processes and delegations of authority;
- enhancing the SEC's operational risk management capabilities; and
- considering potential changes in the SEC's oversight of – and interaction with – self-regulatory organizations.

Since that time, the staff has undertaken an assessment of the recommendations and has provided three reports to Congress detailing the staff activities taken to implement these objectives. Thus far, recommendations and implementation plans have been completed for 15 of the 20 initiatives examined, and the implementation phase is complete or in process for each.

Funding for Implementation of the Dodd-Frank Act[82]

Since passage of the Dodd-Frank Act, the agency's existing staff has worked extraordinarily hard to conduct the large number of rulemakings, studies, and analyses required by the Act. But it has been clear to me from the outset that the Act's significant expansion of the

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[81] The BCG Report is available at http://www.sec.gov/news/studies/2011/967study.pdf.

[82] In accordance with past practice, the FY2013 budget justification of the agency was submitted by the Chairman of the Commission and was not voted on by the full Commission. Therefore, this section of the testimony does not necessarily represent the views of all SEC Commissioners.

SEC's jurisdiction over OTC derivatives, private fund advisers, municipal advisors, clearing agencies, and credit rating agencies, among others, could not be handled appropriately with the agency's previous resource levels without undermining the agency's other core duties. This is proving especially true as we turn from the first step of rulewriting to efforts to support and monitor implementation and the ongoing process of examinations and enforcement of those rules. With Congress's support, the SEC received a FY 2012 appropriation that permitted us to begin hiring some of the new positions needed to fulfill these responsibilities.

Despite this, I believe that the SEC does not yet have all the resources necessary to fully implement the law, and enactment of the President's Budget Request for FY 2013 would be key for filling the remaining gaps. The Request was for $1.566 billion, and it would permit the agency to hire 676 additional individuals. A number of these new hires are needed to focus on enforcement, examinations, regulatory oversight, and economic and data analysis related to the Act.

In FY 2013, the SEC also is aiming to continue investing in its technology capabilities to implement the law and police the markets. In particular, we hope to strengthen our ability to take in, organize, and analyze data on the new markets and entities under the agency's jurisdiction. The enactment of the President's Budget Request, as well as the continued use of the agency's Reserve Fund, will be essential to that effort.

If the SEC does not receive additional resources, I believe that many of the issues to which the Dodd-Frank Act is directed will not be adequately addressed. The SEC would be unable to sufficiently build out its technology and hire the industry experts and other staff sorely needed to oversee and police these new areas of responsibility.

It is important to keep in mind that, under the Dodd-Frank Act, the SEC collects transaction fees that offset the annual appropriation to the SEC. Accordingly, regardless of the amount appropriated to the SEC, I believe that it is appropriate to note that the appropriation will be fully offset by the fees that we collect, and therefore will have no impact on the nation's budget deficit.

Conclusion

The Dodd-Frank Act has required the SEC to undertake the largest and most complex rulemaking agenda in the history of the agency. To date, a tremendous amount of progress has been made to implement that agenda, including significant effort intended to increase transparency, mitigate risk, protect against market abuse in security-based swaps markets, improve the oversight of credit rating agencies and hedge fund and other private fund advisers, and develop a better understanding of the systemic risk presented by large private funds. As the Commission strives to complete the additional work that remains, we look forward to working with this Committee and other stakeholders in the financial marketplace to adopt rules that protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation. Thank you for inviting us to share with you our progress to date and our plans going forward. I look forward to answering your questions.