SPOTLIGHT ON ADVOCACY

TRUMP & CONGRESS TARGET DODD-FRANK DISCLOSURE RULES

The SEC is reviewing its CEO pay ratio and conflict minerals rules.

By Ted Allen

As the Trump administration settles into Washington, D.C., more details are starting to emerge about its regulatory agenda, including the potential rollback of several contentious disclosure rules that were mandated by the Dodd-Frank Act.

While the first month of the Trump administration was marked by high-profile controversies over immigration and foreign relations, comparatively less attention was paid to the new administration's financial regulatory initiatives.

On February 3, Trump signed an executive order that directs the Treasury Department to review Dodd-Frank's impact on the economy. While the president has called Dodd-Frank a "disaster" and vowed to do "a big number" on the law, the process of unwinding the sweeping 2010 statute will take a significant amount of time and likely face opposition from Democratic lawmakers.

The Treasury Department, the Securities and Exchange Commission, and other federal regulators don't have the authority to repeal Dodd-Frank without an act of Congress. The agencies can amend existing disclosure rules and provide some relief to issuers and financial firms, but regulators must go through a formal rulemaking process and could face lawsuits from activist investors who support these mandates.

New Leadership at the SEC

In early January, Trump announced that he would nominate Jay Clayton, a long-time partner with the law firm of Sullivan & Cromwell, to serve as the next chair of the SEC.

Clayton has represented investment banks and issuers in public offerings, mergers, and other transactions. He has never worked as a prosecutor and SEC observers expect that he won't pursue the aggressive "broken windows" enforcement approach of former SEC Chair Mary Jo White.

While several Democrats have criticized Clayton over his representation of Wall Street firms, news reports suggest he has made a good impression on Republicans on the Senate Banking Committee, which oversees the SEC. As of early February, the Senate had not voted on Clayton, but his confirmation was expected.

Until Clayton takes office, the SEC will have just two commissioners – Republican Michael Piwowar, who is serving as acting chair, and Democrat Kara Stein. The evenly divided Commission won't be able to approve any major rule changes unless both Stein and Piwowar agree. In addition, the SEC has two more vacancies that Trump will need to fill to bring the agency up to its full complement of five commissioners. The next SEC chair also will need to select new chiefs to oversee the SEC divisions, including Corporation Finance, which reviews companies' disclosures.

Review of Pay Ratio Rule

In the meantime, Piwowar has started the process for the SEC to delay or pare back two of the Dodd-Frank Act's more controversial mandates. On February 6, he asked issuers to submit comments on the challenges they face in complying with the agency's CEO pay ratio regulation.

Under that rule, most U.S. public companies must report the ratio between the total compensation received by their CEO and that earned by the company's median employee. This calculation may prove quite onerous for many companies, because it is not limited to full-time workers or U.S.-based employees. Issuers are required to report this pay ratio for their first fiscal year that starts on or after January 1, 2017, which means that calendar-year-end companies would make their first disclosures during the spring of 2018.

"However, it is my understanding that some issuers have begun to encounter unanticipated compliance difficulties that may hinder them in meeting the reporting deadline," Piwowar said in a statement. "In order to better understand the nature of these difficulties, I am seeking public input on any unexpected challenges that issuers have experienced as they prepare for compliance with the rule and whether relief is needed."

Those comments are due by late March and Piwowar has urged the SEC staff to promptly review that input and determine whether to provide additional guidance or relief (such a delay in the deadline for the first disclosures).

In comment letters submitted before the pay ratio rule was finalized in 2015, NIRI and other corporate advocates asked the SEC to reduce compliance costs by limiting the scope of the ratio calculation to just full-time, U.S.-based employees. (NIRI encourages members and their companies to submit letters that detail the costs and difficulties involved in meeting this mandate.)

While most IR professionals won't be involved in preparing these pay ratio calculations, they will need to be prepared for investor inquiries and messaging challenges once these disclosures are made. Companies that report significantly higher CEO pay ratios than their peers can expect to face negative news media coverage, employee discontent, and activism by labor pension funds.

Piwowar also has directed the SEC staff to review the agency's conflict minerals disclosure rule, which requires companies to file annual reports on their usage of gold and other minerals from the Congo region of Africa. He voiced concern about the unintended consequences of this "misguided" mandate, which he said had driven legitimate African mining operators out of business.

In addition, the new leadership of the SEC is not expected to advance a trio of draft Dodd-Frank regulations that relate to executive compensation. Those proposed regulations seek to set prescriptive standards for "pay versus performance" disclosures, mandate stricter corporate "clawback" policies, and require companies to disclose their stock hedging policies for directors and employees.

Congressional Action

Meanwhile, Congress has started its efforts to chip away at Dodd-Frank. Invoking the Congressional Review Act, the House of Representatives and the Senate approved a resolution that rescinds the SEC's 2016 rule that directs resource extraction companies to disclose their payments to foreign and state governments. While that resolution, which Trump has signed, doesn't repeal the Dodd-Frank mandate to adopt such a rule, the SEC will be barred from proposing a similar rule for a year.

As of early February, House lawmakers were preparing a new version of the Financial CHOICE Act, a wide-ranging bill that seeks to repeal many Dodd-Frank provisions, including the CEO pay ratio mandate and the conflict minerals rule. That bill likely will include legislation from Representative Sean Duffy of Wisconsin that would direct the SEC to regulate proxy advisory firms. The bill also may call for stricter standards for shareholder proposals.

While Republicans expect that they have enough votes to pass the Financial CHOICE Act in the House, the bill's prospects are less certain in the Senate, where Republicans have 52 seats, short of the 60 votes they would need to overcome a potential Democratic filibuster.

While public companies and IR professionals can hope that they may receive some regulatory relief from Washington, that process won't happen overnight.

"This is not going to be simple, fast, or cheap," former SEC Commissioner Joseph Grundfest, who now is a law professor at Stanford University, told *The Wall Street Journal*. IRU

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