Testimony before the
Subcommittee on Financial Services and General Government
Committee on Appropriations
United States House of Representatives

by Chair Mary Jo White
U.S. Securities and Exchange Commission

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Chairman Crenshaw, Ranking Member Serrano, and Members of the Subcommittee:

Thank you for the opportunity to testify today in support of the President's fiscal year (FY) 2014 budget request for the U.S. Securities and Exchange Commission (SEC).[1] I welcome the chance to discuss how the SEC would make effective use of the $1.674 billion requested for the coming fiscal year and to explain why the agency needs the funding it is seeking to do the job it is required to do on behalf of investors and our capital markets.[2] As described in more detail below, the agency's funding request is critical to support the additional staff, technology, and training needed to fulfill our mission. Even though our funding mechanism is deficit-neutral, I recognize it is critical that we use appropriated funds in the most efficient and effective way possible as stewards of these resources.

As you know, the SEC has a broad, three-part mission: to protect investors, maintain fair, orderly, and efficient markets, and facilitate capital formation. Although I have been at the agency less than a month, two things were immediately apparent: first, the tremendous scope and

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[1] A copy of the SEC's FY2014 Budget Congressional Justification can be found on our website at http://www.sec.gov/about/reports/secfy14congbudgjust.pdf.

[2] The views expressed in this testimony are those of the Chair of the Securities and Exchange Commission and do not necessarily represent the views of the President or the full Commission. In accordance with past practice, the budget justification of the agency was submitted by the Chair and was not voted on by the full Commission.

importance of that mission, and second, the exceptional level of commitment, talent, and expertise the agency's staff demonstrates each and every day on behalf of America's investors and markets. The U.S. markets are the envy of the world precisely because of the SEC's work effectively regulating the markets, requiring comprehensive disclosure, and vigorously enforcing the securities laws. I am honored to have the opportunity to lead the SEC in executing its mission.

Today, the SEC's jurisdiction and responsibilities have evolved to cover significant new aspects of the securities markets. As part of its core responsibilities, the SEC is charged with implementing and enforcing the federal securities laws, overseeing thousands of key market participants (over 25,000 entities currently),[3] and reviewing disclosures and financial statements of approximately 9,100 reporting companies. With the passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) and the Jumpstart Our Business Startups Act (JOBS Act), the agency's importance and scope of responsibilities increased, with the Dodd-Frank Act giving the Commission significant additional responsibilities for over-the-counter derivatives, hedge fund and other private fund advisers, municipal advisors, and security-based swap clearing agencies, and the JOBS Act providing new private offering exemptions, including a new regime for crowdfunding offerings.

[3] These participants include about 10,600 investment advisers, 9,700 mutual funds and exchange traded funds, 4,600 broker-dealers, and approximately 460 transfer agents. We also oversee 17 national securities exchanges, seven active registered clearing agencies, and 10 nationally recognized statistical rating organizations (NRSROs), as well as the Public Company Accounting Oversight Board (PCAOB), Financial Industry Regulatory Authority (FINRA), Municipal Securities Rulemaking Board (MSRB), the Securities Investor Protection Corporation (SIPC), and the Financial Accounting Standards Board (FASB).

In recent years, the agency has made significant strides forward to strengthen its oversight over markets that are so critical to the savings of American families and to the growth potential of American businesses. With the help of the resources provided by Congress in recent years, the SEC has bolstered its examination and enforcement functions, improved its capacity to assess risks, and enhanced its technology. It also has made a number of necessary and important internal improvements designed to maximize efficiencies and reform its operations. Much more, however, remains to be accomplished.

The SEC's current level of resources still presents significant challenges as we seek to keep pace with the growing size and complexity of the securities markets and fulfill our broad mandates and responsibilities. The FY 2014 budget request – all of which would be fully offset by matching collections of fees on securities transactions and thus will not increase the Federal budget deficit – seeks to address these challenges directly, to better position the agency to provide the kind of market oversight that the public expects and deserves.

Before delving into the details of our funding needs for 2014, I would like to briefly highlight a few key areas that I believe should be our top priorities and that have been important drivers for our budget request.

Key Priorities

First, the SEC must complete, swiftly and thoughtfully, the rulemaking mandates contained in the Dodd-Frank Act and JOBS Act. Of the more than 90 Dodd-Frank Act 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 it was directed to complete. But there is still much Dodd-Frank Act work that remains. Similarly, the JOBS Act requires significant Commission rulemaking which has not yet been completed. To fulfill these legislative mandates expeditiously must be an immediate imperative for the Commission. In connection with those rules, I will continue the Commission's efforts to ensure that the SEC performs robust economic analysis, as rigorous economic analysis is important and should inform and help guide our decisions.

While the Commission, with its existing staff, is already far along in many of its statutorily mandated rulemakings, we need additional staff and investments in technology to successfully implement these mandates. For example, the FY 2014 budget request would enable the SEC to bring in more economists to perform economic and risk analyses to assist in all of our rulemaking decisions, as well as support new technology for a municipal advisor registration system. We also need additional resources to improve our ability to help our markets and participants transition to new rules and requirements. Market certainty is critical to its functioning, especially during periods of regulatory change. The FY 2014 request would allow us to hire additional staff with technical skills and experience to process and review on a timely basis requests for interpretations, registrations, and other required approvals. Additional resources also will be needed to help conduct risk-based supervision of newly registered entities such as security-based swaps dealers and major swap participants, which will be subject to registration and regulation by the agency.

Second, I am committed to further strengthening the core enforcement and examination functions of the SEC. Strong enforcement of the securities laws is necessary for investor confidence and is essential to the integrity of our financial markets. Successful enforcement actions result in sanctions that deter and punish wrongdoing and protect investors, both now and in the future. Similarly, our National Examination Program (NEP) is critical to improving compliance, preventing and detecting fraud, and monitoring market risks. As described in more detail below, the current level of resources is not sufficient to permit the SEC to examine regulated entities and enforce compliance with the securities laws in a way that investors deserve and expect.

Third, the SEC needs to be in a position to provide adequate oversight over today's highly complex and dispersed marketplace so that it can be wisely and optimally regulated, which means without undue cost and without undermining its vitality. There must be a sense of urgency brought to understanding more fully the impact on investors and the quality of our markets of high-frequency trading, complex trading algorithms, dark pools, and intricate new order types so that appropriate regulatory responses can be made. I know that many in Congress are also interested in this important area. The FY 2014 budget request would assist the SEC in making investments in much needed technology and expertise, not only helping us keep better pace with the markets we monitor and regulate, but also permitting us to see around corners and anticipate issues that may arise.

FY 2014 Request

The SEC is requesting $1.674 billion for FY 2014. If enacted, this request would permit us to add approximately 676 new staff positions, both to improve core operations and implement the agency's new responsibilities. While we understand that this request comes during a time of serious fiscal challenges, we have tried to be as targeted as we could in making these requests in the areas where the immediate deployment of resources is most critical.

The budget request would provide additional funding for the following key areas:

- expanding oversight of investment advisers and improving their regulation and compliance – a point at which investors are most at risk of being defrauded and harmed;
- bolstering enforcement – a primary function of the agency is to enforce the law and deter other would-be wrongdoers;
- economic and risk analysis to support rulemaking and oversight – critical to good and valid rulemaking;
- building oversight of derivatives and clearing agencies – significant new agency responsibilities to help safeguard against future financial crises;
- enhancing reviews of corporate disclosures – including supporting implementation of the JOBS Act;
- leveraging technology – to improve our ability to detect wrongdoing, streamline our operations, and tighten the security of our data; and
- enhancing training and development of SEC staff – to increase our staff expertise.

I would now like to describe each of these in more detail.

Expanding Oversight of Investment Advisers and Improving Their Regulation and Compliance

During FY 2012, although the SEC continued to use and improve risk-based analysis to select examination candidates in its examination program, it was able to examine only about eight percent of registered investment advisers. Over 40 percent of advisers have never been examined. The number of registered advisers has increased by more than 40 percent over the last decade, while the assets under management by these advisers have increased more than two-fold, more than $50 trillion. In addition to this exponential growth in size, the industry is increasingly complex. This complexity includes: the use of new and sophisticated products, including derivatives and certain structured products; technologies that facilitate high-frequency and algorithmic trading; and complex "families" of financial services companies with integrated operations that include both broker-dealer and investment adviser affiliates. Although the agency has successfully focused its limited examination resources on those areas posing the greatest risk to investor assets, the SEC's examination coverage continues to be insufficient in comparison with the rates achieved by other financial regulators and in the opinion of many third-party observers.

Therefore, under the FY 2014 request, one of the SEC's top priorities is to hire 250 additional examiners to increase the proportion of advisers examined each year, the rate of first-time examinations, and the examination coverage of investment advisers and newly registered private fund advisers. This would be an important step in a multi-year effort to increase coverage by our examination program to meet our regulatory responsibilities to investors who increasingly turn to investment advisers for assistance navigating the securities markets and investing for retirement and family needs.

The NEP also would be able to add 60 positions to improve oversight and examination functions related to broker-dealers, clearing agencies, transfer agents, self-regulatory organizations (SROs), and municipal advisors. In addition, 15 positions would be used to support other critical program initiatives such as enhancing global risk assessment and surveillance efforts and improving technology capabilities. These positions are vital as the agency continues to strive to adapt to the rapid change and increasing complexity of the markets it regulates and its increased examination responsibilities with regard to clearing agencies, securities-based swap market participants, and municipal advisors.

Bolstering Enforcement

The ability to identify and bring timely, high-quality enforcement actions when violations of the federal securities laws occur is integral to the SEC's core mission. The SEC must enhance its enforcement function not only to send strong messages to wrongdoers that misconduct will be swiftly and aggressively addressed, but also to adapt for the highly automated, high-speed, and high-volume markets of today and tomorrow. Under this budget request, we would be able to further refine our analysis of tips and leverage incoming data to identify trends of possible misconduct across product, sector, or geographic areas. We also would engage additional industry experts and proactive data analytics to better target industry practices that may harm investors. For example, we have developed certain algorithms to mine publicly available hedge fund performance data to identify aberrational performance returns that could be indicative of conduct warranting further investigation. With additional front line investigative attorney, trial attorney, and forensic accountant resources, we would further bolster our core work of pursuing potential securities laws violations identified from these and other sources. The Division of Enforcement would focus its hiring of 131 staff on increased expertise in the securities industry and new product areas, trial attorneys, and forensic accountants, as well as staff for the Office of

Market Intelligence, the Office of the Whistleblower, and the SEC's collections and distributions functions.

Economic and Risk Analysis to Support Rulemaking and Oversight

For FY 2014, the SEC requests funding to add 45 positions in the Division of Risk, Strategy and Financial Innovation (RSFI), a roughly 45 percent increase in the size of this essential function. These positions would be used primarily for additional financial economists to perform economic analyses and research in support of the Commission's activities. Specifically, RSFI would seek economists with expertise in analyzing high frequency trading data and market structure and practices, executive compensation and related areas of corporate governance, and credit-default swaps in support of Dodd-Frank Act required rulemakings. RSFI also plans to hire operations research analysts with backgrounds in mathematics, statistics or econometrics to expand the development and delivery of risk metrics and analytics to inform risk assessment in examinations and investigations, rulemaking, and economic analysis.

Building Oversight of Derivatives and Clearing Agencies

The Commission's regulatory responsibilities have been significantly expanded with the addition of new categories of registered entities (including security-based swap execution facilities, security-based swap data repositories, security-based swap dealers, and major security-based swap participants); the required regulatory reporting and public dissemination of security-based swap data; and the mandatory clearing of security-based swaps. To avoid bottlenecks and unintended market disruptions as the new requirements become operational over the next two years, the agency will need additional staff going forward with technical skills and experience to process and review on a timely basis the requests for rule interpretations, registration, or required approvals. New staff also will be needed to supervise registered security-based swap dealers and participants, and to use newly-available data to identify excessive risks or other threats to security-based swap markets and investors.

In addition, the agency intends to focus on further enhancing its oversight of clearing agencies, including clearing agencies expected to register with the Commission in the near future. Currently, six clearing agencies have been designated systemically important by the Financial Stability Oversight Council (FSOC) and, of the six, the SEC is the supervisory agency for four. This has been accompanied by a materially higher level of work, including, for example, an annual exam requirement for the clearing agencies for which we are the supervisory agency and enhanced coordination with other agencies for proposed changes and supervision activities. We also anticipate additional work associated with Commission rules relating to clearing of security-based swaps, as the requirements are new and the relevant clearing agencies are new agency registrants.

Currently, the average transaction volume cleared and settled by the seven active registered clearing agencies is approximately $6.6 trillion a day. Notwithstanding this tremendous volume, the SEC currently has on staff 14 examiners devoted to examining registered clearing agencies, with only a limited on-site presence existing in four of the seven. Additionally, the SEC has about a dozen other staff focused on the monitoring and evaluation of risk management systems used by the existing clearing agencies, and will need to expand these efforts to address the expected increase in the number of clearing agencies and rule filings raising risk management issues. Without these additional resources, the mismatch between the amount of regulated clearing activity and staffing will be exacerbated both by the additional clearing agencies that are expected to register with the SEC as a result of security-based swap activities and the expanded oversight required due to clearing agencies' designations as systemically important by the FSOC. Accordingly, the FY 2014 budget request seeks to add 25 positions in the Division of Trading and Markets and in the NEP to support these functions.

Enhancing Reviews of Corporate Disclosures, Including Supporting Implementation of the JOBS Act

For FY 2014, the SEC requests 25 new positions for the Division of Corporation Finance. These positions would permit us to hire additional attorneys and accountants to continue to enhance the Division's reviews of large companies, review draft registration statements submitted by emerging growth companies under the JOBS Act, prepare and finalize the remaining rules and projects to implement the Dodd-Frank Act and the JOBS Act, and respond to requests for interpretive guidance, including with respect to new rules. Further, the additional positions would allow the Division to enhance its review of SEC rules and regulations impacting small business capital formation and better evaluate trends in increasingly complex offerings.

Leveraging Technology

Beyond the need to increase the number of experts dedicated to overseeing the securities industry, it also is critically important to continue leveraging technology to streamline operations and increase the effectiveness of the agency's programs. While the SEC has made significant progress over the past few years in modernizing our technology systems, the agency must continue to make significant investments if it is to properly oversee the markets and entities it regulates. The FY 2014 budget request would add $56 million for technology to support a number of key Information Technology (IT) initiatives, including enhancements to the system for receiving tips, complaints, and referrals (TCR), improvements to IT security, and infrastructure upgrades to achieve efficiencies in business operations and reduce long-term costs.

The SEC plans to enhance its TCR system by building an interface to the agency's exam and case management systems, adding intake and routing functionality for referrals from the self-regulatory organizations (SROs), and expanding internal reporting to SEC management on the tracking, investigation, and disposition of TCRs. Additionally, the agency plans to develop a component of the TCR system that will automatically triage incoming tips so they can quickly be flagged for additional follow-up.

The agency also seeks to make a significant investment in its information security program to deploy a new set of security tools and develop and train staff to monitor, respond to, and remediate threats. Additionally, the SEC is requesting resources to implement infrastructure upgrades that will achieve efficiencies in business operations and reduce long-term costs. For example, the agency plans a number of initiatives to automate business processes and share data across the agency, to improve collaboration and content management across the agency, and continue strategic replacement of existing hardware and software to hold down maintenance costs.

While the need for resources is significant, we also realize and appreciate the imperative to identify ways to reduce costs wherever possible, so we can dedicate more funds to fulfilling our mission. The SEC has made important strides forward in this regard, identifying and realizing substantial savings and operational efficiencies in recent years. For example, in the technology areas, agency initiatives have resulted in more robust IT infrastructure support contracts, savings in software maintenance and support contracts, upgrades to data storage systems, and reductions in remote connectivity and network costs. Together these steps yielded cost savings of approximately $12 million in FY 2012, and continued savings are expected in FY 2013 and beyond.

The SEC's savings initiatives are expected to continue into FY 2014, as the agency is working to identify and implement new technologies and business process improvements that will offer increased performance with reduced operational costs.

SEC Reserve Fund

In FY 2014, the SEC plans to use $50 million from the SEC Reserve Fund, established by statute, to fund large, multi-year, mission-critical technology projects. As required by statute, we will continue to notify this Subcommittee within ten days of each obligation from the Reserve Fund. Among other projects, the agency would continue its multi-year effort to overhaul the Electronic Data Gathering, Analysis and Retrieval (EDGAR) system to create a new, modernized system that will meet Commission requirements for real-time system updates, reduce filer burden by providing simplified search and filing options based on filer experience (i.e., professional or novice), improve data capture by moving to structured formats for various SEC forms, and reduce the long term costs of operating and maintaining the system.

In addition, we plan to use the SEC Reserve Fund for the construction and enhancement of the Enterprise Data Warehouse (EDW). The EDW is a critical step in combining currently disparate sources of data from EDGAR filings, exam reports, investigations, external vendors, and many other sources. An organized central data repository will allow enhanced analytical capabilities, predictive modeling, and strengthened governance of data controls and quality standards.

We also plan to use the SEC Reserve Fund toward the development of the capability to intake, store and analyze data from the upcoming Consolidated Audit Trail (CAT) that the Commission has mandated the SROs create to increase the data available to regulators. A CAT repository would enable the SEC to intake CAT data and store it in the EDW, as well as to develop analytical tools and a single software platform that will allow the SEC to identify patterns, trends, and anomalies in the CAT data. The tools and platform will allow seamless searches of data sets to examine activity to reveal suspicious behavior in securities-related activities and quickly trace the origin.

Enhancing Training and Development of SEC Staff

The SEC's hardworking staff is the most important component of the agency's successes. The FY 2014 request includes a significant increase in the SEC's total training budget to deepen expertise and skills, in order to keep pace with the rapidly evolving nature of the markets and areas of new responsibility. The planned investment principally supports training and development for employees directly involved in examinations, investigations, fraud detection, litigation, and other core mission responsibilities of the SEC. The training will consist of specialized in-depth training concerning new trends in the securities industry and changing market conditions, the impact of the current market structure on compliance and trading activities, and analytics and forensics using market data. The resources requested in the FY 2014 budget would bring the SEC's level of training investment more on par with other Federal financial regulatory agencies.

Conclusion

I very much appreciate your consideration of the President's FY 2014 budget request. Your support for the SEC's expansive and vital mission will allow us to better protect investors and facilitate capital formation, more effectively oversee the markets and entities we regulate, and build upon the significant improvements we have made to date.

Thank you for inviting me to be here today. I would be happy to answer your questions.