

**MEMO# 19986**

May 1, 2006

## **Testimony of SEC Chairman Cox Before Senate Banking Committee**

©2006 Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice. [19986] May 1, 2006 TO: BOARD OF GOVERNORS No. 16-06 CLOSED-END INVESTMENT COMPANY MEMBERS No. 19-06 SMALL FUNDS MEMBERS No. 37-06 UNIT INVESTMENT TRUST MEMBERS No. 15-06 SEC RULES MEMBERS No. 43-06 RE: TESTIMONY OF SEC CHAIRMAN COX BEFORE SENATE BANKING COMMITTEE On April 25, SEC Chairman Christopher Cox testified before the Senate Committee on Banking, Housing, and Urban Affairs on "Improving Financial Disclosure for Individual Investors."<sup>1</sup> Summarized below are the most significant aspects of the testimony. Chairman Cox stated that the SEC is currently pursuing four key initiatives to improve the quality and usefulness of disclosure for individual investors: (1) making disclosure understandable for ordinary investors; (2) improving disclosure via interactive data; (3) reducing the complexity of accounting rules; and (4) focusing anti-fraud efforts on scams that target older Americans. Making Disclosure Understandable for Ordinary Investors Chairman Cox stated that empowering investors means providing access to better information. He noted that all too often, once SEC mandated information is available to investors, it is not understandable. In addition, even though they are nominally written in plain English, the disclosure in some documents that are provided to investors is often so full of legal jargon and boilerplate disclosure that it can actually obscure important information. Chairman Cox therefore reiterated the importance of providing disclosure to investors in plain English and announced an SEC effort to require plain English in every document intended for retail consumption. <sup>1</sup> Chairman Cox's testimony can be found on the SEC's website at <http://www.sec.gov/news/testimony/ts042506cc.htm>. <sup>2</sup> Improving Disclosure via Interactive Data Chairman Cox stated that the use of interactive data would make SEC mandated disclosures more useful to investors. Interactive data also would provide individual investors with the means to quickly search for any information they want without having to examine a lengthy document. It is envisioned that investors would have access to such information through easy-to-navigate Web pages. Chairman Cox specifically stated that because mutual funds and exchange-traded funds have become the investment of choice for millions of Americans, he is very encouraged that the Institute and its members recently decided to throw their weight behind interactive data. Chairman Cox announced that throughout 2006, the SEC will host a series of roundtables focused on the move to interactive data, the first scheduled for June. Topics that will be discussed include what investors and analysts really need from interactive data; how to encourage the development of software for companies, institutions, and retail investors that takes full advantage of the potential of interactive data; and how to redesign the SEC's disclosure requirements to maximize the advantage of using interactive data. Reducing the

Complexity of Accounting Rules and Regulations Chairman Cox addressed the complexity of the disclosure mandated by SEC rules, specifically accounting rules. He noted that when rules are difficult to interpret, they may not be followed very well and when complexity needlessly adds to the costs and efforts involved in financial reporting, investors often foot the bill. Chairman Cox therefore described several initiatives to reduce the complexity of current accounting rules and regulations. Focusing Anti-Fraud Efforts on Scams Targeting Retirees and Elderly Investors Chairman Cox outlined several SEC efforts to better protect older Americans against financial fraud. He stated that the SEC is attacking the problem from many angles, including investor education, targeted examinations, and aggressive enforcement efforts. Chairman Cox also noted that because state securities regulators share the concern about fraud aimed at seniors, the SEC is cooperating in this initiative with state regulators across the country. Committee Q&As Chairman Cox touched on a number of issues during Q&As from members of the Committee. In response to a question regarding the state of mutual fund disclosure, Chairman Cox again praised the Institute and its members for endorsing the use of interactive data. While praising the Institute's involvement, the Chairman noted that interactive data and the Web are central to SEC efforts to make disclosure more meaningful to investors. Other issues covered at the hearing included: 3 NRSROs Several questions were raised about credit rating agencies and the status of SEC initiatives relating to the reform of the NRSRO regulatory structure. Several members of the Committee noted that reforms are long overdue in this area. Chairman Cox stated that the SEC supports principles that would: avoid erecting new barriers to entry; increase competition; create a transparent registration process; and manage conflicts of interest and prevent the misuse of nonpublic information. He noted that legislation would be necessary for any additional SEC regulation of NRSROs and stated that he is pleased that initiatives in Congress are moving forward to provide such regulation. Hedge Funds Chairman Cox stated that he believes the SEC has adequate resources to regulate the increased number of hedge funds registered with the SEC. He noted that the SEC is specifically training its personnel to properly inspect hedge funds and that there is no delay in the implementation of hedge fund regulation as a result of ongoing legal challenges. The Committee also announced that a hearing on hedge funds will take place on May 16. Requirements of the Sarbanes-Oxley Act The requirements of the Sarbanes-Oxley Act was the subject of a variety of questions. A number of members of the Committee raised concern over major companies choosing foreign exchanges for their IPOs in order to avoid the Act's requirements. Chairman Cox did not indicate whether he favors excluding small companies from Section 404 of the Act although he broadly defended its requirements and said that the SEC is focused on making the requirements work without any unnecessary costs. Regulation of Securities Exchanges Chairman Cox was asked a number of questions relating to the recent structural reform at the U.S. securities exchanges. He stated that the demutualization of exchanges has raised a wide range of issues relating to the regulation of the securities markets and that the SEC is currently examining these issues. Chairman Cox added that the globalization of the securities markets is inevitable and that he will soon be meeting with the U.K. Financial Services Authority to discuss the implications for regulation. Ari Burstein Associate Counsel