Consumer Federation of America

October 5, 2021

The Honorable Maxine Waters
Chairwoman
Committee on Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

The Honorable Patrick McHenry
Ranking Member
Committee on Financial Services
4340 O'Neill House Office Building
Washington, D.C. 20024

Dear Chairwoman Waters, Ranking Member McHenry, and Members of the Committee:

I am writing on behalf of the Consumer Federation of America (CFA) to express support for certain legislation noticed in connection with the House Financial Services Committee's October 5, 2021, hearing on "Oversight of the Securities and Exchange Commission: Putting Investors and Market Integrity First." I appreciate your attention to CFA's views.

A bill to amend the Securities and Exchange Act of 1934 with respect to the Office of the Investor Advocate, and for other purposes. (Discussion Draft)

The SEC Office of Investor Advocate (OIA) was established by Congress "to advise the Commission on regulatory priorities, the regulation of securities products, trading strategies, fee structures, the effectiveness of disclosure, and on initiatives to protect investor interests and to promote investor confidence and the integrity of the securities marketplace."[1] The Dodd-Frank Act authorizes the committee to submit findings and recommendations for review and consideration by the Commission.

As one of the largest consumer advocacy groups in the nation, the Consumer Federation of America is among the strongest allies of the SEC and the SEC's Office of Investor Advocate. Investor protection is a vital component of CFA's overall mission of consumer protection, and CFA therefore seeks to engage the SEC and Congress routinely on securities issues that concern ordinary Americans.

The Discussion Draft referenced above is intended to bolster the ability of the OIA to carry forth is mandate as envisioned by Congress. Among other things, the bill includes provisions that would increase the OIA's independence from the Commission, elevate its voice within the Commission, and lay the foundation for a more robust, sustainable, and comprehensive research function. The proposed reforms are consistent with the spirit and purpose of the OIA, and responsive to a number

[1] SEC, *Spotlight on Investor Advisory Committee*, https://www.sec.gov/spotlight/investor-advisory-committee.shtml.

of specific challenges that the current SEC Investor Advocate outlined for Congress in December 2020.[2]

CFA is pleased to support the bill and looks forward to its introduction and passage.

The Empowering States to Protect Seniors from Bad Actors Act (Discussion Draft)

Senior financial exploitation is an urgent nationwide concern. It is estimated that roughly one in five citizens over the age of 65, or 7 million seniors, have been victims of financial exploitation. Abuses include inappropriate investment recommendations, unreasonably high fees, and outright fraud, costing these older Americans an estimated $2.9 billion.[3] Older Americans are particularly hard hit by such practices, since they are often past the point in their earning years where they can recover those losses. These problems are likely to only intensify with the aging of the "baby boom" generation and with increases to average life expectancies.

State regulators, who form the front line on investor protection for Main Street investors, are an important part of the effort to combat this problem. In recognition of that fact, Section 989(A) of the Dodd-Frank Act established a grant program within the CFPB designed to help state securities and insurance regulators protect this vulnerable population against fraud. The grants were intended for a wide variety of senior investor protection efforts, such as hiring additional staff to investigate and prosecute cases, funding for new technology, equipment, and training for regulators, prosecutors, and law enforcement, and providing educational material to seniors to increase their awareness.

CFA was among those voicing strong support for the program at the time the Dodd-Frank Act was passed.[4] Unfortunately, in the eleven years since the enactment of that statute, the CFPB has been unable to establish this important grant program due to uncertainty about the funding mechanism. The Discussion Draft would fix this problem once and for all by assigning responsibility for the administration of the program to the SEC's Office of Investor Advocate.

CFA strongly supports the bill and urges its swift introduction and passage.

A bill to prohibit registered investment advisers, brokers, and registered representatives of brokers from facilitating the transaction of or recommending the securities of certain special purpose acquisition companies (SPACs), and for other purposes. (Discussion Draft)

This Discussion Draft would amend Section 206 of the Investment Advisers Act of 1940 to make it unlawful for any registered individual to "facilitate the transaction of, or recommend, securities of a special purpose acquisition company, as defined by the Commission, to a person who is not an accredited investor, unless the "promote" to the SPAC is 5 percent or less.

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[2] *See* SEC, Office of the Investor Advocate, *Report on Activities, Fiscal Year 2020*, https://www.sec.gov/files/sec-investor-advocate-report-on-activities-2020.pdf.

[3] *See* U.S. Senate Special Committee on Aging, *Fighting Fraud: Senate Aging Committee Identifies Top 10 Scams Targeting Our Nation's Seniors* 21 (2019).

[4] CFA, NASAA, AARP, and Fund Democracy, *Letter to Senate Banking Committee Chairman Christopher Dodd and Ranking Member Richard Shelby regarding the "Restoring American Financial Stability Act of 2009" Committee Print* (Feb. 2, 2010), https://bit.ly/2QcVQq9.

CFA shares the Committee's view that SPACs need to be more closely scrutinized, including by regulators and policymakers, and has written to the Committee on SPAC issues in the past.[5] We also agree with the premise of establishing a dedicated mechanism with which the SEC could limit retail investors' exposure to the unique risk associated with certain SPACs. At the same time, we believe that the securities laws already afford the SEC significant tools through which to limit or scrutinize risky SPAC deals.

CFA looks forward to working with the SEC and Congress to ensure responsible oversight of so-called "blank check" companies like SPACS. We generally support the proffered discussion draft. We would suggest another avenue that Congress should explore in this regard is legislation that would clarify that liability under Section 11 of the Securities Act applies equally to disclosures made in initial public offerings (IPOs) conducted via mergers and acquisitions as it does to disclosures made in traditional IPOs.

The Investor Choice Act

The Investor Choice Act would prohibit the use of pre-dispute mandatory arbitration contracts in several key areas of the securities industry and regulatory regime. Most notably, the bill would prohibit broker-dealers and investment advisers from including "forced" arbitration clauses in their customer agreements. This will ensure that investors injured by bad actors will be able to bring their meritorious claims in court and would not be forced into a FINRA controlled arbitration forum by nonnegotiable contracts.

The bill would also prohibit issuers of securities from mandating arbitration for a dispute between the issuer and its shareholders in any governing document or contract. This is an important and especially timely reform. While the concept of mandatory arbitration of shareholder claims has been discussed or explored by issuers a few times in the past, during the past several years there has been a concerted push by ideologically motivated shareholders to compel corporate boards to amend bylaws to adopt a mandatory arbitration provision applicable to disputes between a stockholder and the Corporation.

CFA strongly supports the Investor Choice Act.

The Investor Justice Act

In 2018, the SEC's Investor Advisory Committee approved a recommendation calling on the Commission to explore ways to improve external funding sources to the law school investor advocacy clinics.[6] The IAC reasoned that investor advocacy clinics fill a crucial gap for retail investors by providing high quality legal advice and representation to investors would otherwise not have access to representation.[7] At the same time, due to the expiration of a FINRA Foundation grant,

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[5] *See* Americans for Financial Reform and CFA, *Letter to Members of the House Financial Services Committee Re: Special Purpose Acquisition Companies* (Feb. 16, 2021), https://consumerfed.org/wp-content/uploads/2021/02/AFR-Letter-on-SPACs-to-HFSC.pdf.

[6] *See* SEC, Investor Advisory Committee, *Recommendation of the Investor Advisory Committee Subcommittee of the Whole: Financial Support for Law School Clinics that Support Investors ("Recommendation")* (March 2018), https://www.sec.gov/spotlight/investor-advisory-committee-2012/iac030818-law-clinics-recommendation.pdf

[7] According to the SEC IAC, a clinic's typical client tends to be between 60 and 90 years old, elderly, retired or on the verge of retiring and living on their social security income. In addition, most clients are working class investors with \$5,000-\$100,000 in assets invested with a broker. (See Recommendation, P.3)

at the time the IAC considered the matter, a number of such clinics had recently closed. The Committee expressed strong concern that, in the absence of a new source of external funding, many investor advocacy clinics already in operation could be forced to further curtail services or close their doors.

The Investor Justice Act makes good on the recommendation of the IAC and the SEC's Office of the Investor Advocate by authorizing the SEC OIA to award grants, on a competitive basis, to qualified investor advocacy clinics. Under the bill, grant funds could only be used for the development, expansion, or continuation of such a clinic, and would be required to submit a detailed accounting of the use of all grant monies to the OIA. Further, the bill would cap the total amount of grants that could be made for clinics at a maximum of $5 million annually and provides that no single clinic may be awarded more than $150,000 in a given fiscal year.[8]

Investor advocacy clinics that serve retail investors is an excellent example of an instance where a little bit of federal support could do a great deal to benefit a great many investors.

CFA is pleased to support the legislation.

A bill to amend the Securities and Exchange Act of 1934 to improve the governance of multi-class stock companies, to require issuers to make annual diversity disclosures, and for other purposes. (Discussion Draft)

When a company goes public with multiple classes of shares, it allows public investors the opportunity to benefit economically from the company's growth – but it does not allow such investors to exercise the voting rights that shareholders traditionally enjoy as owners of publicly held companies. Typically, this is done to protect the control and interests of the company's founders and executives.

Though there are examples of companies that have utilized multi-class share structures and performed exceptionally well,[9] they are too often the exception. In fact, not only does data suggest that companies utilizing multi-class share structures tend to perform comparatively poorly as investments, but they are also notably more prone to inside dealing and corporate governance failures. Further, the negative implications of multi-class share structures for investors have been exacerbated over the last decade by the advent and increasingly widespread adoption of the so-called "founder-friendly" financing model, which displaced the startup governance structure that was defined by investor control and prevailed until the early 2010s.[10] And finally, perpetual dual- or multi-class share structures require long-term public shareholders to place their faith not only in a founder, but also potentially the founder's children and grandchildren.[11] This mocks the principle of corporate accountability to investors.

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[8] The IAC estimates that that it costs roughly $150,000 to $200,000 per year to run an investor advocacy clinic with at least one full time faculty attorney. (See Recommendation, P.4).

[9] For example, Google and Berkshire Hathaway.

[10] *See* Renee M. Jones, Associate Dean for Academic Affairs and Professor of Law, Boston College Law School, *Written Testimony Before the U.S. House of Representatives, Committee on Financial Services, Subcommittee on Capital Markets, Securities, and Investment* (Sept. 9, 2019), https://financialservices.house.gov/uploadedfiles/hhrg-116-ba16-wstate-jonesr-20190911.pdf.

[11] *See* Robert J. Jackson, Jr., Commissioner, SEC, *Perpetual Dual-Class Stock: The Case Against Corporate Royalty* (Feb. 15, 2018), https://www.sec.gov/news/speech/perpetual-dual-class-stock-case-against-corporate-royalty.

The Discussion Draft would require that newly listed companies that utilize multi-class stock structures agree to a so-called "sunset" provision that would require the dissolution of such share structure not less than seven years from the date of the issuer's initial public offering. The bill would also establish minimum listing standards for exchanges that choose to list the securities of such issuers. Both reforms are sensible and overdue policy responses to a problem that has been allowed to fester for too long.

CFA is pleased to support the legislation.

The Whistleblower Protection Reform Act

The Whistleblower Protection Reform Act would revise Section 922 of the Dodd-Frank Act of 2010 to clarify that whistleblowers who report alleged misconduct to their employers but not also to the SEC are protected by the anti-retaliation provisions in Section 922. The legislation is a necessary response to a 2018 U.S. Supreme Court's 2018 ruling in the case of *Digital Realty Trust, Inc. v. Somers*,[12] which held that only reports made directly to the SEC are protected.

The SEC's Whistleblower Program is an extremely effective tool for uncovering and deterring corporate misconduct. For example, the SEC recently announced that its whistleblower program has now paid more than $1 billion in awards to 207 whistleblowers since its inception, including over $500 million in fiscal year 2021 alone.[13] Despite the Program's continued success, the Supreme Court's 2018 decision undoubtedly opens the door to unfair and unacceptable corporate retaliation against whistleblowers.

CFA is please to support the legislation.

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Thank you for the opportunity to comment on the legislation posted in connection with today's hearing. Should you have any questions, or if CFA may be of any further assistance, please do not hesitate to contact me.

Respectfully submitted,

Dylan Bruce
Financial Services Counsel

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[12] *See* Digital Realty Tr., Inc. v. Somers, 138 S. Ct. 767 (2018).

[13] SEC, *SEC Surpasses $1 Billion in Awards to Whistleblowers with Two Awards Totaling $114 Million*, Press Release (Sept. 15, 2021), https://www.sec.gov/news/press-release/2021-177