



HOUSE FINANCIAL SERVICES SUBCOMMITTEE HEARING

OVERVIEW

For questions on the note below, please contact [Kwon Park](#) at (202) 547-3035.

Yesterday, the House Financial Services Subcommittee on Capital Markets and Government Sponsored Enterprises held a [hearing](#) entitled “Examining the Agenda of Regulators, SROs, and Standards-Setters for Accounting, Auditing, and Municipal Securities.”

Key Takeaways

- Hultgren (R-IL) expressed concerns about options markets and the SEC’s proposed amendments to Rule 15b9-1, requiring certain broker dealers (BDs) to register with FINRA. Colby (FINRA) said that FINRA will respond to industry concerns with ongoing dialogue as the rule gets finalized.
- Kelly (MSRB) explained that the new bond market rule proposal requiring dealers to disclose markups was pursued after careful economic analysis and industry feedback. She said regulators will provide industry enough time to implement systems as this effort necessitates significant technological changes to current systems.
- Garrett (R-NJ) urged FASB and the PCAOB to continue the historical interpretation of the “materiality” standard in SEC filings as they prepare to revise the standard to be consistent with international standards. He also asked regulators, SROs, and standard-setters to incorporate cost benefit analysis into their decision-making.

SUMMARY

Opening Statements and Testimony

[Chairman Scott Garrett \(R-NJ\)](#)

- The PCAOB’s enforcement proceedings lack the due process protections that exist in administrative proceedings at other agencies.
- The long-standing definition and interpretation of the “materiality” standard in SEC filings have worked well and should continue. FASB and the PCAOB should coordinate when revising the definition to be consistent with historical interpretations.
- It is important for regulators, SROs, and standard-setters to incorporate cost benefit analysis into their decisions.

Ranking Member Carolyn Maloney (D-NY)

- Accurate and transparent financial statements are essential for investor protection and to increase confidence in our financial markets.
- The PCAOB publicly disclosing enforcement proceedings (investigations) may harm a firm's reputation before any formal action is taken.

Brad Sherman (D-CA)

- FASB has tremendous government powers – they are funded by tax dollars and can put people in jail. Yet, FASB is not subject to cost benefit analysis, FOIA requests, open meetings, or Senate confirmations for its members.
- FASB's proposed requirement to write off research expenses is a mistake as the \$11 billion appropriated by Congress to incentivize research will be wiped out. This decision violates all of accounting theory and is done solely for the convenience of FASB, and they should revisit this issue.

Ed Perlmutter (D-CO)

- We must focus on how the current regulatory regime impacts small BDs as they are forced to consolidate and merge to survive in today's economy. Small firms insist costs due to PCAOB's audits and supervisory reviews are putting them out of business or troubling them.

Wesley R. Bricker, Interim Chief Accountant, SEC

- The reliability and credibility of financial reporting is critical. The Office of the Chief Accountant (OCA) is focused on the implementation of recently issued accounting standards.
- FASB and ISB are implementing new accounting measures for leasing and a new credit loss standard to increase transparency and to simplify the process for investors.
- OCA remains focused on internal controls of financial reporting – OCA believes updating and maintaining internal financial controls are important.
- Auditors are key independent gatekeepers that protect investors and support PCAOB oversight of firms. PCAOB continues to modernize auditing standards to improve the informative value of reports.

James R. Doty, Chairman, PCAOB

- Accurate and transparent audits are key to investor protection and financial growth. PCAOB remains vigilant and independent, and its auditors are unsung heroes.
- We must foster international cooperation to improve accounting standards. PCAOB has created a center for economic analysis to assess the impact of its recommendations. PCAOB will ask for a small increase in its budget to deal with inflation.

Russell G. Golden, Chairman, FASB

- U.S. GAAP is essential to the functioning of the U.S. economy. Although FASB sets the standards, it does not maintain enforcement authority.

- FASB engages in direct outreach and meets regularly with the industry and regulators to consult with other stakeholders on the consequences of its actions. FASB's broad and inclusive process helps to assess issues and to strike the right balance.
- FASB's future agenda includes finding solutions for the following issues: intangible assets including research and development, pensions and other postretirement benefit plans, distinguishing liabilities from equity, and reporting performance and cash flows (including income statement, segment reporting, other comprehensive income, and statement of cash flows).

Jessica Kane, Director of the Office of Municipal Securities, SEC

- The municipal advisor registration rule recently passed, and implementation is ongoing.
- The Office of Municipal Securities (OMS) is focused on market structure initiatives for the municipal securities market. Chair White identified the following recommendations:
 - Assure that brokers are subject to meaningful obligations to achieve best execution for investors;
 - Help investors better understand the cost of their fixed income transactions; and
 - Focus on a regulatory initiative to enhance the public availability of pre-trade pricing information in fixed income markets.
- OMS remains focused on compliance with continuing disclosure requirements of Rule 15c2-12 and disclosure practices more generally.

Lynette Kelly, Executive Director, MSRB

- MSRB has made significant strides to provide investors, states, and local issuers with an unprecedented level of municipal market transparency.
- MSRB has enhanced transparency with new tools and resources on its website and continues education initiatives for issuers and investors alike.

Robert L. D. Colby, Chief Legal Officer, FINRA

- The municipal securities market is overseen by the MSRB, SEC, and FINRA. Effective coordination is achieved by leveraging resources and collaborating on many topics.
- FINRA oversees BD compliance in municipal securities actions and examines registered municipal advisors through coordination with MSRB and the SEC.
- FINRA's fixed income market proposal requires additional pricing information to be disclosed to customers to better enable comparisons across products.

Discussion

Rule 15b9-1 - FINRA Registration Proposal

Hultgren (R-IL): What is the potential impact to options markets if the rule was finalized without changes? Why would registration improve option markets – as the rule's scope seems broader than intended? *Colby:* The rule's purpose is to expand FINRA oversight into entities trading in specific markets to ensure they are included in the broader audit trail that FINRA currently operates. We have

spoken to market participants and hope to respond to industry concerns with pending proposals, including possible fee reductions.

Money Market Fund Rule

Hultgren (R-IL): Has the cost benefit analysis of the rule shown increased costs on borrowings for issuers? *Kane:* These amendments are scheduled to become effective this October. Many factors determine an investor's decision on where to allocate capital, and the low interest rate environment might be playing a role.

Bond Market Transparency and Liquidity

Schweikert (R-AZ): Have fee disclosures on municipal bonds improved? *Kelly:* MSRB fiduciary duty rules apply to BDs and municipal advisors and prohibit obsessive charges. State rules also make bond fee disclosures more transparent (i.e. attorney fees are disclosed).

Neugebauer (R-TX): The new proposal makes dealers disclose markups – what are the pros and cons of this proposal? Should increased disclosures show liquidity profiles? *Kelly:* After two years of comments and economic analysis, we decided to pursue markup disclosure. FINRA and MSRB filed rule proposals with the SEC, and it is currently in the notice and comment process. The effective date will be 12 months after the SEC approves the rule. Significant technological changes are needed, so we want to ensure enough time for industry to implement systems. MSRB launched a free website that provides information on over 1.3 million individual municipal securities. Liquidity is part of our economic analysis.

Hultgren (R-IL): Does Congress need to take steps to clarify the rule's intent? *Colby:* We have seen situations where firms act as advisers and underwriters.

Scott (D-GA): Are there any emerging threats to municipalities? Any threats to using municipal bonds to build mega-stadiums? *Kane:* MSRB requires registration for municipal bond advisors, and they are subject to fiduciary duty standards to protect against conflicted advice. Another focus has been on compliance with continuing disclosure obligations. Funding mega-stadiums via municipal bonds are completely up to the local government.

Maloney: Describe enforcement actions in municipal markets and whether they will become emerging threats? *Kane:* We have a specialized unit for municipalities in the enforcement division; *Colby:* We have brought cases on undisclosed markups and failure to report transactions.

Treasury Trade Reporting Proposal

Maloney: Where does this rule stand? *Colby:* We filed a proposal to require members to disclose the audit trail of treasury securities and hope the SEC approves our recommendations shortly. Public reporting dissemination of treasury data is a question for the Treasury Department and the SEC. We simply responded to the request to develop the audit trail.

“Materiality”

Garrett: FASB is issuing guidance to revise the “materiality” standard – explain FASB's logic of updating the definition and upholding its historical interpretation? *Golden:* We want to align the new definition

with the existing interpretation, as well as to update the definition to ISB standards; *Doty*: We are consulting other agencies to ensure auditors are complying with the legal standards that the SEC and FASB decides to establish.

Poliquin (R-ME): Does FASB perform cost benefit analysis? *Golden*: Yes.

PCAOB

Garrett: If there is a PCAOB enforcement proceeding against a firm, would an investor want to know?

Doty: Absolutely. However, the investigation stage should remain confidential.

Maloney: When will you submit a budget request? *Doty*: November 30. Our request will be the same as last year with adjustments for inflation, etc.

Sherman (D-CA): If an investigation against a firm is announced and the firm is found innocent, would it hurt the firm's reputation if this is made public? *Doty*: Yes. Investigations should remain confidential.

Ellison (D-MN): Any benefits to section 404b of Sarbanes-Oxley for investors? *Doty*: Yes, good internal controls are the best tools for early detection of problems and to prevent fraud.