OVERSIGHT OF THE SEC'S DIVISION OF ENFORCEMENT

HYBRID HEARING

BEFORE THE

SUBCOMMITTEE ON INVESTOR PROTECTION, ENTREPRENEURSHIP, AND CAPITAL MARKETS

OF THE

COMMITTEE ON FINANCIAL SERVICES

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TUESDAY, JULY 19, 2022

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ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

OVERSIGHT OF THE SEC'S DIVISION OF ENFORCEMENT

Tuesday, July 19, 2022

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON INVESTOR PROTECTION,
ENTREPRENEURSHIP, AND CAPITAL MARKETS,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10:03 a.m., in room 2128, Rayburn House Office Building, Hon. Brad Sherman [chairman of the subcommittee] presiding.

Members present: Representatives Sherman, Scott, Himes, Foster, Vargas, Gottheimer, Axne, Casten; Huizenga, Wagner, Hill, Emmer, Mooney, Davidson, Hollingsworth, and Steil.

Ex officio present: Representative Waters.

Chairman SHERMAN. The Subcommittee on Investor Protection, Entrepreneurship, and Capital Markets will come to order.

Without objection, the Chair is authorized to declare a recess of the subcommittee at any time. Also, without objection, members of the full Financial Services Committee who are not members of the subcommittee are authorized to participate in today's hearing.

Today's hearing is entitled, "Oversight of the SEC's Division of Enforcement."

I now recognize myself for 4 minutes for an opening statement.

There is nothing more important for this subcommittee to do than oversee the SEC. I look forward to the Full Committee bringing the Chair of the SEC before the Full Committee. I would hope that would happen either at the subcommittee level or at the Full Committee level several times each year. But oversight of the SEC is also enhanced by bringing before us the Division Director of the largest division of the SEC.

The Securities and Exchange Commission oversees $100 trillion in securities investments, and reviews disclosures of 7,400 public companies, including more than 4,000 exchange-listed public companies. The SEC has an annual budget of $2 billion, supporting 4,500 employees across both the headquarters and the 11 regional offices, the most important of which is now in my new district in Los Angeles. The Agency's largest division is the Enforcement Division with some 1,366 employees, representing a quarter of the SEC staff. The Division is responsible for enforcing our securities laws. In 2021, the SEC filed some 434 new enforcement actions, representing a 7-percent increase.

As the Chair of the SEC, Gary Gensler, pointed out, the purpose here is to discourage misconduct before it happens. Today, the Divi-

sion faces new challenges in the form of cryptocurrencies and other digital assets. The combined value of these digital assets hit $3 trillion at their peak, from which it has declined. In response, in 2017, the SEC established the Crypto Assets and Cyber Unit within the Division of Enforcement. That Division has brought some enforcement actions related to fraudulent and unregistered crypto asset offerings and platforms, resulting in monetary relief totaling $2 billion. This is by far the most of any Federal or State regulatory body.

Obviously, there have been recent downturns in the purported value of crypto assets. In particular, their enforcement actions depend upon the definition of the word, "security," under a relatively ancient Howey Test. The Division has determined that XRP is a security and is going after XRP, but for reasons that I will bring up in questions, has not gone after the exchanges where tens of thousands of illegal securities transactions were occurring.

The Division faces a number of longstanding challenges. Today, we are considering a number of important bills that are listed for all of the members of this subcommittee and are being considered in this hearing. There is no Federal statute defining, "insider trading." I know Mr. Himes has a bill designed to do just that. And, of course, the *Newman* decision narrowed the definition somewhat of, "insider trading." Another issue for us to confront is the maximum civil monetary penalties, which some bad actors simply regard as a cost of doing business.

A recent decision in the Fifth Circuit has called into question the use of administrative law judges (ALJs), which is the primary method of enforcing our securities laws. The Court found a number of problems. Some are constitutional and would require a change in practice if that court decision, which is now on appeal to an en banc review, is upheld. But other concerns of the Court are about the inadequate standards that the Congress has put into the statute, and we need to correct those by legislation, probably even if the Court decision is successfully appealed. Finally, we are looking at the SEC's use of waivers, where bad actors admit to wrongdoing but then don't face the full penalties.

With that, I recognize the ranking member of the subcommittee, the gentleman from Michigan, Mr. Huizenga, for his 5-minute opening statement.

Mr. HUIZENGA. Thank you, Mr. Chairman, and welcome, Director Grewal. I'm glad to see you here. And interestingly enough, it has been 4 years since the Director of Enforcement was sitting where you are today, 4 years since the subcommittee provided oversight for your Division, and 4 years since members of this committee on both sides of the aisle were given the opportunity to raise concerns over enforcement actions taken by the SEC. I think it is safe to say this hearing is long overdue. This hearing is entitled, "Oversight of the SEC's Division of Enforcement," which is a key element of what this subcommittee's jurisdiction is, and it has been missing.

And I appreciate the efforts of the Chair, who has been advocating, at least privately with us, about having you and other Directors and frankly, even having the Chair of the SEC. But this is not going to stop the request from myself and, I think, from other members of this committee. This is a constitutional requirement

and duty to act as the oversight for the Administration at all levels.

The SEC has come a long way in the last 4 years. And in that 14 months since you were sworn into office, Chair Gensler has charted a path for the SEC unlike any other time in its 88-year history, from an Agency that has a mission to protect investors; to maintain fair, orderly, and efficient markets; and to facilitate capital formation, those three things. Let me repeat that: protect investors;—we all agree on that—maintain fair, orderly, and efficient markets;—we all agree on that. But to facilitate capital formation seems to be something that has fallen off of his radar in many ways. And he has embarked on one of the most ambitious rulemaking agendas in our modern era, since we have had the SEC.

Let's put this in perspective. The SEC's past three Chairs issued half as many proposals in their first 14 months compared to the current Chair. The flurry of activity is evidence that the rapidly-evolving enforcement and regulatory landscape at the SEC is an indicator of things to come. I don't think it is going to slow down.

In the past, increased enforcement activity at the Commission has signaled that they will act aggressively, pressing the boundaries of their enforcement authority. Look no further than the SEC's announcement this past May to nearly double its Crypto Enforcement Unit. While the Commission does not intend to provide any clarity surrounding the application of securities laws to digital assets, the unit plans to focus on violations related to crypto asset offerings, so crypto asset exchanges, crypto asset lending and staking products, decentralized financial platforms, non-fungible tokens, stablecoins, et cetera, et cetera. It is worth mentioning that of the 63 items included in the Agency's rulemaking agenda this past spring, there is actually zero pertaining to digital assets.

In addition to the Division's proactive enforcement efforts—your words not mine—the SEC continues to use its own administrative law judges (ALJs) to adjudicate enforcement actions, a controversial decision that has been used increasingly over the past decade. In a recent court decision, the Fifth Circuit Court of Appeals noted that Congress unconstitutionally delegated legislative power to the SEC when it allowed the Commission to decide when to use these ALJ's, coupled with the SEC's admission earlier this year that there was a control deficiency related to the separation of the SEC's enforcement and adjudicatory function, with serious ramifications regarding the fairness of prior SEC enforcement actions for the party subject to those actions.

Finally, I would be remiss if I didn't mention the one person who is not here this morning, the Chair of the Securities and Exchange Commission, Chair Gensler, but I know he is paying attention. So, Chair Gensler, I appreciate you allowing Director Grewal to come before the subcommittee, but I can't help but mention your absence and request your attendance.

Mr. Chairman, I would like to submit two letters from Ranking Member McHenry and myself, one dated October 6, 2021, and the other May 5, 2022, requesting Chairwoman Waters to hold a hearing with all 5 of the SEC Commissioners. It has now been nearly 3, 4 years since we last heard from the Commission, and since

then, Chair Gensler has proposed 23 rules that await adoption. I think it is long overdue.

And Director, let me caution you with this last word. We should not evaluate the true effectiveness of the regulatory agency or its enforcement program solely based on how many headlines it can generate. That is true of any Federal or State regulatory agency in the country, and it is certainly true for the SEC. And I look forward to hearing from you on the impact on our capital markets. With that, I yield back.

Chairman SHERMAN. Thank you. I now recognize the Chair of the full Financial Services Committee, the distinguished Chairwoman Waters.

Chairwoman WATERS. Thank you, Chairman Sherman, for holding this important hearing. Between last year's main stock events, the employees in Special Purpose Acquisition Companies (SPACs), and this year's catastrophic crypto crash, the life savings of ordinary Americans who were drawn into risky and fraudulent investment schemes have been lost. The work you do every day to go after scammers and those who peddle unsuitable financial products is critical. It is refreshing and promising to have as our witness today Director Grewal, an Enforcement Director who fought for years as an Attorney General on behalf of the people of New Jersey.

Director Grewal, welcome to the committee, and thank you for your years of public service.

Chairman SHERMAN. Thank you. Today, we welcome the testimony of our distinguished witness, Mr. Gurbir Grewal, who is the Director of the Division of Enforcement at the Securities and Exchange Commission. Previous to that, he was the Attorney General of the State of New Jersey.

Director Grewal, you are reminded that your oral testimony is limited to 5 minutes. You will see the timer. You know the drill. And without objection, your full written statement will be made a part of the record.

Also without objection, the letters referred to by the ranking member will be made a part of the record.

Director Grewal, you are now recognized for 5 minutes.

STATEMENT OF GURBIR S. GREWAL, DIRECTOR, DIVISION OF ENFORCEMENT, U.S. SECURITIES AND EXCHANGE COMMISSION (SEC)

Mr. GREWAL. Chairman Sherman, Ranking Member Huizenga, Chairwoman Waters, and members of the subcommittee, good morning, and thank you for inviting me to testify today on behalf of the SEC's Division of Enforcement.

Since its founding more than 85 years ago, the SEC has stayed true to its three-part mission of protecting investors; of maintaining fair, orderly. and efficient markets; and facilitating capital formation. Central to that mission is the work of the Enforcement Division. Since my appointment, I have been amazed by the talent and the expertise of the Division staff, and I am privileged to call them all my colleagues.

Each year, the Commission brings hundreds of enforcement actions and obtains meaningful relief on behalf of the investing pub-

lic, and Fiscal Year 2021 was no exception. Despite the challenges of the global pandemic, we filed 434 new enforcement actions, covering a broad range of violations and representing a 7-percent increase over the prior fiscal year. Yet, many Americans' trust in our financial markets and institutions is at near historic lows. While there is no single cause for that decline, part of it is certainly due to repeated lapses by large institutions and gatekeepers, and the perception by many that they are not being held accountable. It is critical that we at the Enforcement Division do our part to restore that trust and to increase accountability. And I believe that is best done by focusing on three things: robust enforcement; robust remedies; and robust compliance.

Robust enforcement means investigating and litigating every type of case within our remit with a sense of urgency. It also means keeping pace with new areas of importance for investors, as well as continually-evolving risks. That is one reason we recently added 20 positions to our Crypto Assets and Cyber Unit. The expanded unit will leverage the Agency's expertise to ensure investors are protected in the crypto markets and against cyber-related threats.

Robust enforcement also means focusing on gatekeepers such as compliance officers, accountants, and attorneys. We can't be everywhere, and gatekeepers are often the first lines of defense against misconduct. So when they fail to live up to their obligations, their professional responsibilities, and when they give cover to corporations or executives engaged in misconduct, investors and market integrity suffer and trust deteriorates.

A second component of restoring trust is seeking robust remedies in our cases. Put simply, the remedies we seek must both punish wrongdoers and deter those violations from happening in the first place. To ensure that is the case, we are constantly assessing what penalties in prior comparable cases have sufficiently deterred the misconduct at issue. Where they haven't, especially recidivists, we will seek stiffer penalties.

Robust remedies must also include obtaining all appropriate prophylactic relief available, such as bars, suspensions, conduct-based injunctions and undertakings, and relief, which directly protects investors and market integrity by preventing violators from engaging in future misconduct. And while most of our cases will continue to include no-admit, no-deny settlements, we will seek admissions from wrongdoers in certain cases, especially in cases where heightened accountability and acceptance of responsibility are in the public interest.

Finally, robust compliance is also critical to restoring trust. We are in a time of rapid and profound technological change. Public companies and other market participants need to think rigorously about how their specific business models and products interact with both emerging risks and their obligations under the Federal Securities Laws. And they must tailor their internal controls and compliance practices and policies accordingly. In short, they must work to foster a culture of proactive compliance and responsibility. To ensure that is the case, we are pushing enforcement actions that go to the heart of robust compliance efforts, including actions

targeting wholesale recordkeeping failures by firms that have either promoted or failed to rein in off-channel communications.

All of what I have described requires resources. As the number of enforcement employees has decreased over time, we have faced significant and mounting challenges which are described in more detail in our budget requests and in my submitted testimony. At the same time, many of our investigations are becoming more and more difficult as fraudsters find new ways to communicate.

Our Fiscal Year 2023 budget seeks additional staff to enable us to meet these mounting challenges and to maintain an effective investigative capacity and deter presence for the benefit of our markets and investors. I am confident that with adequate resources, and by emphasizing robust enforcement remedies and compliance in our work, we will be able to meet future challenges, achieve our tripartite mission, and do our part in restoring public trust in our financial markets and institutions.

Thank you for inviting me today, and I look forward to answering your questions.

[The prepared statement of Director Grewal can be found on page 32 of the appendix.]

Chairman SHERMAN. Thank you, and I now recognize myself for 5 minutes for questions.

I will point out that Chairman Gensler came before our full Financial Services Committee twice last year, and he will be coming before us, I believe, later this year. More is better, but we are certainly doing our job. The ranking member points out that the SEC has a number of regulatory projects. I commend them for having those projects, because as the ranking member points out, we need clarity. If anything, we need another project, and that is to define a security, particularly with regard to the digital world. I would also point out that investor protection is the very best thing we can do for capital formation. It may be a hassle for the individual issuer, but when we build a system where investors are confident, that is what causes people in this country to invest in growing businesses.

My first question relates to spring-loaded stock options. The SEC has analyzed these as to whether they are insider trading. I would like you to focus on whether they are, in effect, a fraud on shareholders in their annual filings. They filed a statement saying that they have a stock option plan in which stock options are going to be granted at fair market value on date of grant. If it is 6 p.m., before the next day, you are going to make the big announcement, and you look at the market price with the market not knowing about your upcoming big announcement. You can say, well, that is the market value, because that is what ignorant shareholders bought and sold the stock at. And the Compensation Committee got approval for granting the stock option at fair market value. They know the fair market value is going to skyrocket the next day because the big announcement is coming.

Why are you not enforcing against spring-loaded stock options when shareholders are defrauded when they are told that the option will simply give the grantee a share in future appreciation after option grant date?

Mr. GREWAL. Thank you for the question, Chairman Sherman. I can't comment on specific investigations that may or may not exist at this moment. I would agree that your hypothetical raises serious fraud concerns. The facts that you have laid out would implicate accounting issues on how those options are being accounted for, and they would implicate disclosure issues. As you mentioned, what did the issuer disclose in its filings? What did it say about how—

Chairman SHERMAN. I would hope you would go back and look at the many instances of spring-loaded stock options, particularly when, in the headline, the shareholders who are asked to approve these plans, are making knowledgeable plans, told that the option exercise price is going to be fair market value on the option grant date. And then, they may define fair market values as what the market closed at, which is usually true, except the market closed right before the big announcement.

I want to move on to another question. You have gone after XRP because XRP is a security, but you haven't gone after all of the major crypto exchanges that process tens of thousands, if not far more transactions. If XRP is a security, and you think it is and I think it is, why are these crypto exchanges not in violation of the law? And is it enough that the crypto exchanges have said, well, having committed tens of thousands of violations in the past, we promise not to do any more in the future? Is that enough to get you off the hook for enforcement?

Mr. GREWAL. Again, I can't talk about what matters we are looking at or not looking at. We have brought exchange cases. We brought one last year against Poloniex. I share your concerns that if the securities are—

Chairman SHERMAN. It is easier to go after the small fish than the big fish, but the big fish operating the major exchanges did many, many tens of thousands of transactions with XRP. It is a security, which means that they were illegally operating a securities exchange. They know it is illegal because they stopped doing it, even though it was profitable. So if they know it is illegal, and you know it is illegal, and I know it is illegal, I hope you focus on that.

And then finally, we have Tether, which is a money market mutual fund in every way. It broke the buck. I realize you are reluctant to talk about individual matters, but can you tell us why you went after Terra, but not Tether?

Mr. GREWAL. Again, it would be inappropriate for me to comment on who we are going after or not going after, but I understand your concerns. And we have added resources to our Crypto Assets Unit to look at issues that put investors at risk, including the issues you have raised in your questions.

Chairman SHERMAN. And fortitude and courage as well. You are going to have to take on some cases that you are not certain of winning.

I now recognize the ranking member of the subcommittee, the gentleman from Michigan, Mr. Huizenga, for 5 minutes.

Mr. HUIZENGA. Thank you. And Director Grewal, like I said in my opening statement, we want to see more of you, not less of you. I will note to the Chair that, yes, the Chair of the SEC was in front of this Full Committee in October. But look at what has happened

since October with the rulemaking, the number of proposals, et cetera, et cetera. And unless there is some secret plan to make sure he is here in September, he is not going to be here, maybe not even for the rest of this Congress, which would be over a year since we have seen the Director.

Director Grewal, I am concerned about a couple of things, and I am going to try to hit this quickly: one, unprecedented attempts by the SEC to slip drastic market changing interpretations of securities laws into otherwise routine enforcement cases; and two, the lack of internal consistency when it comes to the SEC's own ideas about basic foundational elements of market regulation.

In a recent case, the SEC, rather than relying on decades of existing case law and legal precedent, presented a case in which it defined a, "dealer," as, "any business that purchases and sells securities for its own account." So if I am interpreting this correctly, it quite literally means that every market participant in the country, under the SEC definition, regardless of their business model or current regulatory regime, would somehow now be subjected to a wildly different, and inappropriate, in my opinion, regulatory framework, that quickly, overnight. And that is not all. At the same time, in the same SEC, there is a controversial proposal under way in which the SEC is attempting to dramatically expand the definition of this core term, "dealer," but this time, in a wholly different manner than how your Enforcement team defines the term.

So, two different definitions being presented by the same SEC are, in fact, wholly inconsistent with each other. It seems to me that the SEC is frankly brazen about it, and thinks that it can rewrite the most basic elements of securities law whenever it wants, to fit whatever purposes it needs at the current moment, with no regard to the effect on markets, the economy, or even internal consistency.

I am a guy from Michigan, so I think in car terms, right? This is a little like we are asking people to buy a car, but we won't tell them what the speed limit is going to be. We won't tell them what the car should or shouldn't do, what safety products ought to be on it, but we are going to determine that later, and we are just going to mail you a ticket for speeding. We have a responsibility to set speed limits and/or then to make sure that there is a consistent approach and application of that. Could please illuminate me on this approach?

Mr. GREWAL. Thank you for that question, Ranking Member Huizenga. With respect to the enforcement action that you referenced, that is a litigated matter, and we are confident that our position will survive scrutiny in that litigation. We have succeeded in another—

Mr. HUIZENGA. How about the inconsistency of it?

Mr. GREWAL. I can't speak to the rulemaking. That is being done by the Rulemaking Division, and I think it is in a different context. I would refer you to my colleagues in those divisions who are responsible for that rulemaking.

Mr. HUIZENGA. If we could get them here, I would love to ask them. I want to return to something I brought up during my opening remarks about the the administrative law judges (ALJs). As you know, the SEC announced in April that they had identified a

control deficiency related to the separation of its enforcement and adjudicatory functions within its system for administrative adjudications. To quote an article from The Wall Street Journal, "It is the equivalent of a party in litigation having access to a judge's briefs from her law clerks." Given the scrutiny that the SEC has received over the use of their ALJs, I find this breach very concerning. Quickly, Director, can you assure members of this committee that the cases brought before an ALJ during that time of the breach were fairly adjudicated?

Mr. GREWAL. Again, with respect to the breach, as soon as that breach was discovered, it was reported, and it was publicly reported, and the matter is under investigation right now internally. But importantly, no Enforcement Division personnel were found to have access to those materials. It was simply that there were some permissions that allowed people to do so, but not access—

Mr. HUIZENGA. And what gives you that confidence? Has there been an investigation to determine that?

Mr. GREWAL. It is underway right now, Ranking Member Huizenga.

Mr. HUIZENGA. Then, how can you say that there was no breach? You actually don't know if the investigation is still going on.

Mr. GREWAL. Excuse me. I am sorry to talk over you. In the announcement that the Commission made—again, it is not being handled by my Division; it is being independently investigated—it was indicated that the materials weren't accessed. The investigation is going to cover how this lapse happened in the first place.

Mr. HUIZENGA. Has the SEC Office of Inspector General reviewed this incident?

Mr. GREWAL. I would direct you to the Office of Inspector General. I am not aware of what they are looking at or not looking at.

Mr. HUIZENGA. I will be following up with some additional questions in writing as well, but this underscores the importance of this, so I appreciate it. Thank you.

Chairman SHERMAN. I now recognize the gentlewoman from California, the Chair of the Full Committee, Chairwoman Waters, for 5 minutes.

Chairwoman WATERS. Thank you very much. Director Grewal, as you know, I have been focused on the problems associated with the lack of clear fiduciary standards for broker-dealers going back to the days when we were debating and drafting the Wall Street Reform and Consumer Protection Act. After the financial crisis, I continued to believe that brokers providing investment advice need to clearly put the interests of their customers ahead of their own. This fiduciary standard is the gold standard to which all financial professionals who offer personalized advice to investors must adhere.

Former SEC Chair Clayton, despite opposition from investors, approved the flawed Regulation Best Interest (Reg BI). Calling something, "best interest," doesn't make it so. For example, it relied excessively on disclosure to cure deep conflicts-of-interest problems. It allowed brokers to place their interests at par with those of the investors. Under Chair Gensler's leadership, and your leadership of the Division of Enforcement, the SEC for the first time enforced Reg BI. The case you brought forward showed that between July 2020 and April 2021, Affirm and its brokers rec-

ommended and sold certain bonds to senior investors with limited financial wherewithal. While the issuer of the bond had clearly stated that the bonds are high-risk and suitable for those with substantial financial resources, I can't imagine only one firm or a handful of brokers are engaging in these kinds of practices and harming investors.

Director Grewal, I know you can't talk about specific cases, but please do describe your experience in enforcing Regulation Best Interest. Also, please address how, if at all, the broker-dealers have changed their practices? How are they better managing conflicts of interest? For example, do they offer the kinds of products and get paid at the same level that they did prior to Reg BI?

Mr. GREWAL. Thank you for the question, Madam Chairwoman. As you know, Reg BI became effective on June 30, 2020. And after it became effective, there was a period of educating the market, and then our Division of Examinations went and conducted exams with a priority focus on looking at Reg BI compliance. That examinations process yielded a number of referrals, including the case you have referred to, which was our first Reg BI action. It is a litigated action against a broker-dealer and five of its registered reps for selling highly-illiquid debt securities to elderly retirees where it didn't fit with their investment profile. So, that matter will be litigated. There are other referrals. Exams in its 2022 priorities has also indicated that it will be going out to look for compliance.

And to answer the questions you raised, is it having its intended effect, is it changing behavior, or are broker-dealers addressing conflicts of interest, it remains to be seen. But it is my hope that with enforcement actions, with education, and with compliance, that it is having its desired effect in the market.

Chairwoman WATERS. Thank you very much. Director Grewal, as you know, nearly two-thirds of capital raised through our capital markets nowadays is done under various exemptions of the securities laws. These securities are not registered with the SEC, and investors in these securities, including pension funds, university endowments, foundations, and other large funds do not benefit from the protection provided by the securities laws and the rules of the SEC. For example, investors often do not have access to audited and timely financial statements of the issuer of benefit from certain conflicts-of-interest provisions that apply to brokers that market these unregistered securities. Separately, but related, I am also concerned that foreign issuers, including foreign hedge funds and private equity funds that raise capital in the United States, take advantage of these exemptions. And I am concerned that U.S. regulators don't know who invests in these funds or where these funds are themselves in this.

Chairman Sherman and I have been working on legislation to increase transparency into this exempt offerings market. In the America COMPETES Act that the House passed earlier this year, there is a provision that would require issuers of exempt offerings to provide a basic level of information to the SEC, including the beneficial owner of the fund and in which country the fund intends to invest the proceeds of the offering.

I am over my time at this point, and you don't have to respond to this right now, but I will be getting back to you to talk about this issue. And I yield back the balance of my time.

Chairman SHERMAN. Thank you. I now recognize the gentlewoman from Missouri, Mrs. Wagner, for 5 minutes.

Mrs. WAGNER. Thank you, Chairman Sherman, and Ranking Member Huizenga. Director Grewal, the SEC is expected to finalize its proposal on mandatory climate disclosures in the coming months. Issuers will be required to disclose very detailed and scientific climate-related data, possibly including data on downstream Scope 3 emissions such as production and transportation of goods, employee commuting, and a host of other indirect missions. Operationally, sir, how do you plan on handling enforcement cases involving an issuer's disclosure of its Scope 3 emissions?

Mr. GREWAL. Thank you for that question. Again, the rulemaking process is being run out of—

Mrs. WAGNER. I am talking about the enforcement.

Mr. GREWAL. Yes, I will speak from an enforcement perspective. We will take the same approach we have taken to date. We know that ESG and climate issues are important to investors. We know that issuers are making statements about their climate risk already, and we know that investment advisers are marketing ESG funds. We brought greenwashing cases when they breached their fiduciary duty on the adviser side. We brought cases against issuers, most recently, a litigated case against Brazilian issuer, Vale, for lying about its ESG policies. And it is the same thing: if we find that sort of deceit in their statements, we will bring a case.

Mrs. WAGNER. But how will the SEC verify whether the issuer has misstated its Scope 3 emissions?

Mr. GREWAL. Again, I can't speak to the climate rulemaking—

Mrs. WAGNER. From an enforcement standpoint?

Mr. GREWAL. —but how we are doing it in our enforcement actions, is we are relying on experts in our litigating matters.

Mrs. WAGNER. Experts? Really? Is the SEC an expert in climate policy?

Mr. GREWAL. We have retained experts in our case to litigate that matter.

Mrs. WAGNER. You have?

Mr. GREWAL. Yes.

Mrs. WAGNER. What statute provides the SEC with the direct authority to regulate climate change?

Mr. GREWAL. In the litigated matter, there are violations of the anti-fraud provisions of the Federal Securities Laws. That is a theory in the litigated case.

Mrs. WAGNER. And you say the SEC has experts on staff to address climate change?

Mr. GREWAL. Again, I can't speak to the rest of the SEC. I could just talk to—

Mrs. WAGNER. But you just did. I am just asking. Do they have—

Mr. GREWAL. I am just talking about my Enforcement Division and the people we have retained in that particular case as experts.

Mrs. WAGNER. You have experts?

Mr. GREWAL. We have retained them in the litigation, yes.

Mrs. WAGNER. How will the SEC recruit and hire qualified staff who are both experts on climate change, in your purview, and securities law disclosures?

Mr. GREWAL. Our attorneys and investigators are the experts on the securities laws, and we consult with experts in our investigations and in our litigation, regardless of the subject. In the particular example I am sharing with you, we rely on experts on the types of issues that—

Mrs. WAGNER. Perhaps we need to bring those, "experts on climate change in the SEC," before this committee. Director Grewal, when it comes to enforcing the SEC's ESG disclosure rule, how do you envision determining whether a fund has incorporated ESG factors into its investment selection process when the SEC has not defined and likely cannot define just what those factors are?

Mr. GREWAL. Again, I don't want to speak to the rulemaking. I would refer you to—

Mrs. WAGNER. I am not speaking to the rulemaking. I am saying there is no definition. How do you do enforcement?

Mr. GREWAL. The tools we have, you are talking about advisers. We brought a case recently against BNY Mellon for misstating their ESG practices. They said they were conducting ESG review before making certain investments, and it turns out they weren't abiding by the processes that they had made out in their disclosures—

Mrs. WAGNER. Reclaiming my time, sir, just how are these funds expected to know what the letters, "ESG," even mean without a clear definition in the proposed rule, and how will the Enforcement Division know what the letters, "E," "S," and "G," mean without a clear definition?

Mr. GREWAL. Again, in the adviser space, in that particular case, we alleged a violation of the anti-fraud provisions of the Advisers Act. We alleged a breach of the advisers' fiduciary duties because they misstated to the investing public what they were doing when it came to how they were—

Mrs. WAGNER. Has the SEC put out a definition of, "ESG?"

Mr. GREWAL. Again, I think that is what the rulemaking process is—

Mrs. WAGNER. But you can't enforce something that is not defined, sir.

Mr. GREWAL. Representative Wagner, you can enforce lies, when the adviser lies about what it is doing.

Mrs. WAGNER. Lies, when they don't even know what the clear definition in the proposed rule is. We really need some answers on this. Mr. Chairman, I hope that we can bring in some of these so-called SEC experts, and I am highly disappointed in the lack of answers and transparency today. I yield back my time. Thank you.

Chairman SHERMAN. Thank you. I now recognize the gentleman from Georgia, Mr. Scott, who is also the Chair of the House Agriculture Committee, for 5 minutes.

Mr. SCOTT. Thank you, Mr. Chairman. I appreciate that, and welcome, Director Grewal. But first, I want to set the record straight. This whistleblower program has been very, very effective, and I want to commend Chair Gensler and our SEC for the excellent job they are doing. The program has brought violations using

whistleblower information. It has resulted in $5 billion in monetary sanctions, rewards totaling $1.2 billion. The program deteriorates crime, it places fraudsters in jail, and it protects the integrity of our capital markets, so job well done.

Now, I want to make sure that you have the proper funds, the money to continue to do the fine work that you are doing. My first question is this, Mr. Grewal: Can you guarantee that the whistleblower program is now properly equipped, and properly funded to process the current number of complaints with the money that you have, and hold these fraudsters accountable?

Mr. GREWAL. Thank you, Representative Scott, for that question. Our whistleblower program is critical to our enforcement program. The information that whistleblowers provide about wrongdoing sometimes allows us to bring actions that we otherwise wouldn't be able to make. We have dedicated more resources to more timely-resolved whistleblower applications. The number of applications is increasing, but we are investing the resources to make sure that the program remains the success that it is now.

Mr. SCOTT. Let me ask you this, I think that you and the SEC are requesting for your budget for Fiscal Year 2023, an 8-percent increase over the Fiscal Year 2022 budget. I understand that this will go towards an increase of 12.5 new positions for the Enforcement Division, is that correct?

Mr. GREWAL. I think it is 125.

Mr. SCOTT. 125, with 20 new positions for crypto assets, is that correct?

Mr. GREWAL. I think—

Mr. SCOTT. And your Cyber Unit?

Mr. GREWAL. I believe that is accurate.

Mr. SCOTT. And 90 new positions for the Division of Examinations. Can you share with us how many of these enhanced staffing increases will be solely focused on the whistleblower program?

Mr. GREWAL. I think it will depend, Representative Scott, on what we ultimately receive as part of the budget process, but I can assure you that we have put resources in already. We continue to put people in on detail, and we continue to find ways to give them the resources they need to do their work. But it is a priority for us, and we try to balance that with all of our other priorities.

Mr. SCOTT. So, you are telling us that this will be adequate funding for you to continue?

Mr. GREWAL. Yes.

Mr. SCOTT. Okay. Now, let me briefly discuss the SEC's recently-proposed amendments aimed at enhancing the rules governing its whistleblower program. The first proposed amendment would allow the SEC to pay whistleblower awards for actions brought by other entities. The second amendment would uphold the SEC's authority to consider increasing the dollar amount of an award, but not lowering it. Why do you believe, Mr. Grewal, that adopting these changes is critical to continuing to protect our whistleblowers?

Mr. GREWAL. The changes you discussed, Representative, I think are important in recognizing what whistleblowers bring to our investigations, that it is not just the SEC, but sometimes, also parallel Department of Justice (DOJ) investigations, or parallel investigations by other regulators that result in recoveries that should

be considered in the process when we are determining what a whistleblower award is.

Mr. SCOTT. Thank you again, Director Grewal. My time has expired. Continue to do the great job that the SEC is doing with this vitally important and needed whistleblower program.

Mr. GREWAL. Thank you.

Chairman SHERMAN. Thank you. The Chair has been advised that there will be votes on the House Floor sometime between 11:00 and 11:30. My hope is that we will be able to conclude the hearing before we actually have to cast the votes. And I will now recognize Mr. Hill from Arkansas for 5 minutes.

Mr. HILL. Thank you. Director Grewal, thanks for coming before us today, and I want to follow up on a couple of comments from Mrs. Wagner's questions. In the BNY Mellon enforcement case on greenwashing, can you share with the committee who the experts were that your litigation team consulted with on that case, or did you have any in that particular case?

Mr. GREWAL. That is not the investigation I was referencing.

Mr. HILL. You were talking about the Brazilian dam situation?

Mr. GREWAL. That is right.

Mr. HILL. Yes. Okay. Let me turn to BNY Mellon. The allegation there was, as they said, that they had a process by which they determined if companies were eligible to be in an ESG fund, and, in your view, they just didn't follow it, so they were misleading. Is that a fair assessment?

Mr. GREWAL. That is what they admitted to as well.

Mr. HILL. Yes. And that would tell me that you have all of the authority you need as it relates to protecting investors in the mutual fund ESG arena using simply the power you have now. Is that fair? You can go in and make a judgement if someone is misleading in advertising, either at the financial advisor level or at the fund-sponsor level. Is that fair?

Mr. GREWAL. I would agree that the anti-fraud provisions we have that allow us to bring these cases are adequate. Again, the rulemaking is not my division, but what the rulemaking will help with is putting all of those disclosures in a consistent, comparable format that would allow us to more easily further our investigations.

Mr. HILL. I have been looking at the proposed rule and reflecting on how that might provide clarity if you were then going to pursue an enforcement case, and I have a couple of comments on that topic. Have you read the recommendations of the Task Force on Climate-related Financial Disclosures that was chaired by Mark Carney and promoted by Mike Bloomberg? Have you read that 2017 document?

Mr. GREWAL. I have not, Representative.

Mr. HILL. Because it outlines many of the things that I think Chair Gensler and some of my colleagues on the other side of the aisle say are very important. And one of those—again, Representative Wagner raised Scope 3 emissions, and Scope 3 emissions is in that proposed rulemaking, is it not?

Mr. GREWAL. I believe it is, yes.

Mr. HILL. Yes. Thank you. Let me read you what the task force says about trying to do this. "The gaps in emissions measurement

methodologies, including Scope 3 emissions and product lifecycle emissions methodologies, make reliable and accurate estimates difficult. The lack of robust, cost-effective tools to quantify the potential impact of climate-related risks and opportunities at the asset or project level makes aggregation across the organizations activities or an investment portfolio problematic and costly. The need to consider the variability of climate-related impacts across and within different sectors and markets further complicates the process and magnifies the cost of assessing potential climate-related financial impacts. And finally, the high degree of uncertainty around the timing and magnitude of climate-related risks makes it difficult to determine and disclose the potential impacts with precision."

That is what the Carney/Bloomberg task force says about trying to deal with Scope 3. How in the world could the SEC have that in a rulemaking?

Mr. GREWAL. Again, I would have to refer you to the Policymaking Division—

Mr. HILL. We will do that, but how do you think, as an enforcement officer, you could take that to court? Challenging? Yes or no?

Mr. GREWAL. Again, I haven't read the report you are talking about, and I try to—

Mr. HILL. Just read the proposed rulemaking that your Agency has put forward because it has the same philosophy, that this is a no-brainer, and we need to do it to save the planet. So, I am asking you, can you enforce something that is vague, not reliable, not accurate, not timely, not comparable across industries, not comparable within the industry, and not agreed upon by the accounting profession, those companies, or your staff? It's pretty hard to take a case to court on that, yes or no?

Mr. GREWAL. Again, I haven't looked at the report you are talking about, and I will share your concerns with the Policymaking Division. I try to explain how we go about our enforcement actions.

Mr. HILL. Right. We are grateful for your enforcement service. And a lot of us on both sides of the aisle share the greenwashing concerns about misleading advertising by the biggest fund companies in the country, and we have studied that. We have heard testimony here about funds that allegedly are sustainable funds, but they actually look just like an S&P 500 fund, but charge a higher fee. Is that what you have seen in some of your research on litigation?

Mr. GREWAL. We have seen that type of misrepresentation certainly in the matter that we talked about today. And again, I can't talk about other investigations that we are looking at in this space, but it is a concern when investors are not getting accurate information about what they are investing in.

Mr. HILL. We thank you for your service to the people of New Jersey, and now the people of the United States. I yield back.

Mr. GREWAL. Thank you.

Chairman SHERMAN. Thank you. I think we all agree with the gentleman from Arkansas that clear standards are helpful. That is why I am pleased to recognize the gentleman from Connecticut, Mr. Himes, who is the author of the Insider Trading Prohibition Act, which would codify and define, "insider trading." He is also the Chair of our Subcommittee on National Security, International De-

velopment and Monetary Policy. Mr. Himes is recognized for 5 minutes.

Mr. HIMES. Thank you, Mr. Chairman, and welcome, Director Grewal. And since the chairman teed me up for it, I will just note that in your written testimony, you say something very important. You say many Americans' trust in our financial markets and institutions is at near historic lows, quoting a Gallup poll. And then, you go on to say that some believe that there are two sets of rules: one for the big and powerful; and another for everyone else. That, I think, is accurate and should concern us. And I think it does concern people on both sides of the aisle here.

Maybe I will just point out that my bill, H.R. 2655, the Insider Trading Prohibition Act, has now passed through Congress, has been included as an amendment to the NDAA, and it is time for it to become law. I am grateful to my Republican colleagues for making that bipartisan. Now, of course, we just need to get it through the United States Senate. I do appreciate your Agency's assistance on that. I think it is important, given all that you have to do, that your enforcement people not spend a whole lot of time slicing and dicing *Newman* and *Solomon,* and that we finally do what we should have done long ago, which is, if we are going to prosecute people, make it clear precisely why we are prosecuting them. But I do thank you and your Agency for the assistance there.

In my remaining time, Director, I have been focusing quite a bit, as I know you have, on cryptocurrency, and I have a question for you. I have watched the ramping up of both people and resources on that side. I wonder, given the list of names—Tether, Voyager, Excelsior, et cetera, et cetera, et cetera—where we have seen really substantial either declined bankruptcies or questions around fraud, do you have the resources and the expertise that you need? Even if the answer to that question is, "yes," what more does the SEC need in this maybe paused excitement around cryptocurrency to make sure you are in a position to enforce?

There is a second question I want you to ask that may be a little bit less comfortable, which is I am pleased that the Congress is really working hard in educating itself on cryptocurrency and even moving some legislation. So, this may not be a comfortable question for you, but since you have the panorama of misbehavior and make decisions about when to enforce and not to enforce, what advice would you give us as lawmakers for what should be at the top of our priority list in terms of legislating?

Mr. GREWAL. I will start with the first question on resources. Certainly, resources are an issue across our Division and across the Agency. We are still not up to the numbers we were at prior to 2016. The additional resources in the Crypto Asset Unit will help. They include litigators, because a number of these cases are in court right now and are a drain on our resources, but the expertise is not within Enforcement alone. We rely on Finnhub, which is our strategic hub for finance and innovation technology, and we rely on other divisions and their expertise. So, it is a team effort on these issues as they touch the other divisions.

I think we will need more resources moving forward. But for the time being, I think this will allow us to focus on all of the risks that we are seeing right now in the market that you alluded to in

your question, and to continue our investigations on pace to make sure investors are protected, and those that aren't compliant with our laws come into compliance.

With respect to the second part of your question, I would be happy to sit down with your staff and talk through some of the issues that we are seeing in a different setting, and go through some thoughts that we may have on that. I just need to consult with others because, again, it is not just an enforcement issue alone.

Mr. HIMES. Let's talk for a second. It is a nice opportunity to address a lot of people who are thinking about and working on this, so let me push you on that a little bit. Obviously, we are doing a lot of thinking here about how you divide the world between the SEC and the Commodity Futures Trading Commission (CFTC). I don't have a lot of time, but maybe talk a little bit about partnership cooperation. How is that going? Is there anything, again, as we draft legislation, that we should bear in mind?

Mr. GREWAL. Not just with respect to crypto, but there are a whole host of other spaces in which we work well with the CFTC, and we run into them where issues may touch both of our remits, and we know how to deconflict. We know how to work in parallel. We did that. With the collapse of the Archegos family office, they brought charges that touch on their remit. We brought charges that touched on our remit. The Southern District of New York (SDNY) brought criminal charges. We did that with the collapse of infinityQ in other cases, so we know how to work with them. We work well together. And the Chair has alluded to some areas in which we could use additional guidance, and I would defer to the Chair's office on those issues.

Mr. HIMES. Thank you, Director. My time has expired.

Chairman SHERMAN. Thank you. I now recognize the gentleman from Minnesota, Mr. Emmer.

Mr. EMMER. Thank you, Chairman Sherman, and Ranking Member Huizenga, for hosting this hearing today. Mr. Grewal, you frequently acknowledge that public trust and confidence in our capital markets is eroded. In fact, on October 13, 2021, you stated, "The decline in trust undermines the investor confidence needed for the fair, efficient, and orderly operation of our capital markets. Put simply, if the public doesn't think the system is fair, they are not going to invest their hard-earned money." I agree, but time and time again, you placed the cause of blame for this erosion of trust almost squarely on the shoulders of industry participants and companies.

Mr. Grewal, the SEC is in no way blameless here. Chair Gensler's political regime at the SEC, carried out by its Division of Enforcement, has been characterized by a focus on using enforcement to expand SEC jurisdiction at the expense of public resources, public investment in our country, and public trust in our markets. It seems clear to everyone, except maybe those at the Commission, that the SEC is not regulating in good faith. Although many sectors of the industry have grappled with the SEC's politicization of regulation over the last 14 months, it can be seen most clearly when it comes to the digital asset industry.

Take, for example, industry sweeps. As you know, industry sweeps are not novel to the digital asset industry. They are a series of voluntary document production request letters that a regulator sends to everyone in a given industry who is similarly situated or is involved in the same type of activity. Mr. Grewal, does the SEC Division of Enforcement do industry sweeps?

Mr. GREWAL. We do industry sweeps from time to time when we have an—

Mr. EMMER. Thank you. The answer is, "yes." I reclaim my time. Are there currently any industry sweeps underway?

Mr. GREWAL. I'm sorry. I can't talk about investigations on our public—

Mr. EMMER. You can't talk about it legally or you won't talk about it?

Mr. GREWAL. It is our policy not to confirm or deny investigations.

Mr. EMMER. So, you won't talk about it. Okay. What do you do if a company, sir, cannot respond to a sweep letter because they are not in your jurisdiction?

Mr. GREWAL. If we issue a voluntary request for information, there is not much we can do. We can proceed with the subpoena and then a subpoena enforcement action.

Mr. EMMER. So, you do extraterritorial jurisdictional requests?

Mr. GREWAL. Voluntary requests are just that. They are voluntary. They are an important part—

Mr. EMMER. Again, sir, I am not asking about the request now. I am asking about the people you direct those to. There are some that would be within the SEC's jurisdiction, and there are some that are not. My question is, and I think you have confirmed it, that you do industry sweeps to extraterritorial jurisdictional market participants, people you do not have enforcement authority over?

Mr. GREWAL. We subpoena individuals and witnesses who may be in the market, market participants—

Mr. EMMER. Are they within your jurisdiction and outside of your jurisdiction?

Mr. GREWAL. We are not limited by our jurisdiction. When we are collecting evidence, we follow the evidence wherever it leads to and to whomever it leads. There may be someone who doesn't work in the—

Mr. EMMER. I would say, sir, or I would ask you, so you do extraterritorial jurisdictional work. Someone argued that that is not appropriate. But Mr. Grewal, has Chair Gensler ever directed you, or to your knowledge as to any of your colleagues, to make it a bloodbath for companies who don't respond to a sweep letter, which are voluntary?

Mr. GREWAL. No, that has not happened.

Mr. EMMER. Interesting. We have become aware that Chair Gensler has in the past directed the Division of Enforcement to send a sweep letter to a particular sector of the crypto community designed to jam them into a violation that is allegedly unconstitutional. And if any company does not respond to said sweep letter, which I will reiterate, as you said several times, are supposed to be voluntary, then the SEC would make it a, "bloodbath," for them.

If true, I imagine such a tactic would significantly erode trust between the public and the SEC.

Here is the problem. The SEC isn't interested in clarifying what areas of the crypto industry fall under SEC jurisdiction. We know that because Finnhub, which you have referred to, the SEC Division focused on crafting crypto regulation, has essentially dissolved under Chair Gensler. Nonetheless, while abandoning good-faith attempts to clarify how the Commission's existing authority applies to digital assets, the SEC is hell-bent on expanding the size of its Crypto Enforcement Division and using enforcement to unconstitutionally expand its jurisdiction.

Under Chair Gensler, the SEC has become a power-hungry regulator, politicizing enforcement baiting companies to, "come in and talk to the Commission," then hitting them with enforcement actions and discouraging good faith cooperation. Understand, sir, there is a new day coming. Thank you. I yield back.

Chairman SHERMAN. I now recognize the gentleman on the screen, Mr. Vargas from California.

Mr. VARGAS. Thank you very much, Mr. Chairman, and I thank the ranking member for this hearing, and, in particular, thank you, Director Grewal, for being here.

Director Grewal, last year Congress passed my ESG Disclosure Simplification Act which would require public companies to disclose certain environmental, social, and governance (ESG) matters in annual filings with the Securities and Exchange Commission. Investors in my district and across the country have increasingly been demanding that public companies disclose ESG material that is material and informs their market activity. As a result, the SEC has received thousands of comments from the economists, market advocates, and investors requesting that companies and banks file ESG disclosures to protect investors, ensure fair, orderly, and efficient markets, and facilitate capital formation.

Therefore, I am glad that the SEC has proposed an ESG rule that clarifies reporting standards, "to promote consistent, comparable, and reliable information for investors concerning funds and advisers in cooperation in environmental, social, and governance factors."

Director Grewal, can you please describe how your Division is positioned to enforce this rule, once implemented, and ensure that investors have access to standardized ESG disclosures?

Mr. GREWAL. Thank you, Representative Vargas, for the question. As I mentioned earlier, the rulemaking is done by different divisions than mine.

Mr. VARGAS. Okay.

Mr. GREWAL. It is impossible for me to talk about climate enforcement pursuant to those rules because they haven't been adopted, and the version of the final rule hasn't been put out. What I could tell you is that we have seen from the enforcement perspective that ESG issues are certainly important to investors, and that greenwashing is occurring. We are using the tools available to us, the anti-fraud provisions of the securities laws to hold bad actors accountable, whether they are issuers who are making material misstatements about climate risks or about their ESG strategies,

or advisers who are doing the same thing. We are holding them accountable under the Advisers Act.

Mr. VARGAS. You have been using the anti-fraud provisions, but they do seem a little bit inadequate. I think that is why they are coming up with the rules. Is that the reality?

Mr. GREWAL. Again, I would have to refer you to the Rulemaking Division, but I think you mentioned it at the beginning of your question. It is to have in one format consistent, comparable information when the issuers are speaking on these issues or when advisers are speaking on these issues, so that consistency will help us evaluate compliance. And if people are lying about their compliance with those regulations, then certainly that is something we would look at, but it is hard to talk about the rules before they are proposed or before they are made final.

Mr. VARGAS. That is a good point, but you did talk about lies. You can enforce lies. In fact, you said that companies have already confirmed that they had lied in cases. So, you were able to go after them under the anti-fraud provisions with respect to ESG?

Mr. GREWAL. That is right. We brought some recent actions, both in the adviser space and against issuers.

Mr. VARGAS. I was a little curious here when you said that, obviously, you have experts in the law. Those are your lawyers, and you do have very good lawyers, but you said that you rely on experts for the environment or ESG matters, I believe that you said experts outside of the SEC. Are those regular experts that you use in litigation, let's say, but you wouldn't in medical purposes, but an attorney would rely on experts bringing their case. Is that what you mean? Is that the type of expert you are talking about?

Mr. GREWAL. That is exactly right. That is something we frequently do in this space and other spaces where we need litigation experts, where we need to qualify experts for court proceedings, where we need to produce expert reports on litigation-related matters. That is right.

Mr. VARGAS. I would commend you, again, for working in this ESG space. I think it is very important. I do think that many investors see that as material, which is what matters, and, again, I appreciate you doing that. Lastly, I do want to comment very briefly on the issue of cryptocurrency. I can't believe that you are getting criticism for an industry that basically has almost collapsed and has taken so many retail investors down. I appreciate what you are doing. I know you need more people in that section, and I am happy to support you in that. I have 13 seconds left, 12 seconds, and I just say again, thank you for showing up. We appreciate you, and I think you are doing a great job. Thank you.

Mr. GREWAL. Thank you.

Chairman SHERMAN. I thank the gentleman from California for his observation, and I now recognize Mr. Davidson of Ohio for 5 minutes.

Mr. DAVIDSON. Thank you, Mr. Chairman. Thanks for finally holding this really important hearing, and thankfully, our colleague, Mr. Vargas, doesn't give investment advice, particularly with respect to the crypto market. And thankfully, we can clarify some of the things here.

I just want to clarify that I think enforcement is a very important function for the SEC. So, thank you, and those who are committed to doing it honestly and ethically as part of our government at the Securities and Exchange Commission. But fundamentally, are digital assets exempt from treatment as pump-and-dump scams?

Mr. GREWAL. No. We have seen pump-and-dump schemes involving digital assets.

Mr. DAVIDSON. How many enforcement actions have been taken by the SEC?

Mr. GREWAL. Again, I would have to provide you that information at a later date.

Mr. DAVIDSON. I would appreciate that.

And frankly, I am curious why some of the biggest ones that look, to an outsider, like probably pump-and-dump scams don't get targeted? It seems like some things are given a pass and some things are targeted. What is the criteria for targeting?

Mr. GREWAL. There is no selective prosecution. We have to balance the risk that we are seeing with the resources that we have, and we have a number of investigations.

Mr. DAVIDSON. And maybe the big ones take too many resources to go after, so you just say, you will get a pass?

Mr. GREWAL. No, I am very proud of the work that the 1,300 women and men in my Division do. They don't give people a pass. They hold violators accountable.

Mr. DAVIDSON. Okay. Let me run a hypothetical scenario by you, whereby an SEC official gives a speech at a conference. And the official begins, of course, by stating that, "their views are their own and not necessarily those of the Commission." Anyone who has ever heard an SEC official speak would know that this is standard and they would not interpret the speech as legal guidance. However, let's say that the SEC official consulted SEC staff, and perhaps even ethics directly, to assist them in writing the speech or giving guidance. Under this scenario, would the written speech still be considered personal views of the individual and not views of the Commission?

Mr. GREWAL. Respectfully, I can't answer that right now, because that hypothetical is a real scenario that is playing out in litigation.

Mr. DAVIDSON. Oh, what litigation would that be?

Mr. GREWAL. That would be the *KRipple* litigation

Mr. DAVIDSON. Ripple XRP. Is it true that Director Hinman submitted his speech to ethics for approval?

Mr. GREWAL. Again, I can't comment on pending litigation.

Mr. DAVIDSON. Okay. Director Grewal, we talked a little bit about the SEC. Last year, the SEC made a quote: "no action enforcement announcement regarding the amendments to proxy advisor rules from July 2020." Further, the financial services and general government appropriations bill moving through the Rules Committee this week prohibits any funds from being used to implement these proxy adviser rule amendments. On July 13th, Chair Gensler even announced that the SEC would consider adopting different amendments to the rules governing proxy voting.

Given that regulation by enforcement is Chair Gensler's specialty, I find it ironic that the Agency refuses to enforce the al-

ready-settled proxy adviser rules. Here, we have regulatory clarity and, yet, no enforcement. When it comes to digital assets, we have zero clarity, yet the Commission chooses to regulate by enforcement selectively, it appears, frankly. Can you please explain this Gensler paradox?

Mr. GREWAL. Again, I can't speak to the rulemaking. That is being handled by a different division as is the exemptive relief—

Mr. DAVIDSON. The rulemaking on proxy advisors is clear. It is already the law. Why aren't you enforcing it?

Mr. GREWAL. Again, our Division doesn't engage in selective enforcement. We have over 1,500 investigations—

Mr. DAVIDSON. So, you just aren't actively commenting because there is active enforcement going on of that rule?

Mr. GREWAL. I am responding to the statement that we are selectively—

Mr. DAVIDSON. No, no, I want you to respond to my question. Is there active enforcement of the standing proxy adviser rule?

Mr. GREWAL. Again, I am not going to talk about investigations that may or may not exist. It is our policy that investigations are confidential, so—

Mr. DAVIDSON. There is a specific one, but are there other actions to enforce the existing law?

Mr. GREWAL. We enforce the Federal securities laws when we see violations. We have 1,300 women and men who investigate those violations, and when we make a recommendation to the Commission, and they agree with our recommendation to move forward with an enforcement action, we do. When a matter is settled, we recommend that settlement to the Commission.

Mr. DAVIDSON. Okay.

Mr. GREWAL. We are doing everything we can to hold violators accountable, so I have to push back because—

Mr. DAVIDSON. I think we will disagree about performance. I am glad you are here. Director Grewal, as you know, U.S. capital markets boast nearly 41 percent of global equity and 40 percent of global fixed income. Needless to say, we have the deepest, most-robust capital markets in the world. Was it that way prior to Chair Gensler taking over at the SEC?

Mr. GREWAL. I think the Chair has constantly recognized how robust our capital markets are.

Mr. DAVIDSON. Okay. So, it was that way before. I think he has recognized that he didn't make our markets great. They were that way before and continued to be that way despite his presence, or maybe in spite of his presence here. Do you believe Chair Gensler will ever stop pursuing a social-political agenda in weaponizing securities law—

Chairman SHERMAN. The time of the gentleman has expired, but he is welcome to submit his question for the record, and I am sure our witness will give him a good written response.

I now recognize the gentleman from Illinois, Mr. Casten, who is also the Vice Chair of this very subcommittee.

Mr. CASTEN. Thank you, Mr. Chairman. And thank you, Director Grewal. I want to ask you a couple of questions, if I could, more on the investor protection realm. It is a little over the 2-year anniversary of the death of Alex Kearns from Naperville, Illinois. This

was the young man who was told by Robinhood that he owed them $730,000, then took his own life after writing his parents a note saying that he didn't know how someone who only had $5,000 to his name was allowed to trade $730,000 of options. That story was soon eclipsed in the national zeitgeist by the GameStop hearings and getting into where were the incentives within Robinhood.

And what emerged on this committee was that Robinhood is really this sort of near perfectly toxic brew of selling only to people where they have payment for order flow (PFOF) contracts, earning their revenue not as a fixed fee on those PPF contracts, but as a percent of the spread, the bid ask spread, on the back end and then relying on gamification. So, they just have these incentives to find the least-sophisticated money in the market, connect them to the most-sophisticated players, and then basically use gamification to put the whole thing on steroids.

We have had a number of hearings in this committee. We have had a number of bills. I wonder if you could just speak for a moment about what the SEC is doing specifically around gamification and payment for order flow, because as I sit here, we still have not created the regulatory conditions that will protect a future Alex Kearns from being caught up in this same toxic brew. Can you speak briefly to that?

Mr. GREWAL. First, I am sorry to hear that about the constituent. It is a horrible, horrible story, and I have read about it. Gamification is a huge concern. Last year, in the fall, we put out a request for information about gamification, and we are trying to gather more details from people across the market to see how this practice exists, and get different perspectives on that practice. And my hope is that will help inform our next steps.

From an enforcement perspective, I am concerned when gamification crosses the line into a recommendation. If it does, then those folks have to comply with Reg BI. And I see that as a potential avenue for us to get involved in that space, and we are concerned about it. And gamification also, I think, as we have seen, can be used for further manipulative conduct, and so is a concern from an enforcement perspective as well.

Mr. CASTEN. You have touched exactly on my follow-up. This format is horrible, because we want to play, "gotcha," and get zingers on the record. But at least as I sit there, from my perspective, I have no idea how you could honestly say you were looking out for the best interests of your customers if you are using gamification to recommend stocks and if you are only relying on payment for order flow off takers, right? By definition, you are not looking, and can you say anything affirmatively that we know this?

And it hurts me because we are 2 years in, in what seems to be obvious, and we are still waiting for a hearing and a ruling. Meanwhile, companies like Robinhood continue to make a lot of money from what seems to be not looking after their investors' best interests.

Mr. GREWAL. Again, I can't talk about specific entities or individuals or firms that we may or may not be looking at. I could tell you that digital engagement practices more broadly are a concern for the Chair. We started this information-gathering last fall on this issue. Perhaps, that will inform future rulemakings. I have

shared with you how I think it impacts enforcement. It is something that we are very concerned about, particularly with Reg BI, how it intersects, and couldn't constitute a recommendation. And then on the manipulation side, how it could be used in furtherance of manipulative conduct, and it could have horrific consequences as well, as we have seen in the case that you highlighted.

Mr. CASTEN. I know I only have 50 seconds left here, but the crypto rise and crash looks an awful lot like the meme stock rise and crash. It is driven by a lot of the same zeitgeist that, again, looks like the unsophisticated players taking charge. Leaving aside that, you can't tell us exactly what you are doing on the gamification and P5 issue? Is crypto the same way, or we are going to have to at some point clarify whether you or the CFTC has authority over crypto before we can make sure that we are protecting those investors there?

Mr. GREWAL. We are using, Congressman, our authorities to investigate and bring actions against those who violate our laws, whether they be the anti-fraud provisions or other aspects of the securities laws.

Mr. CASTEN. Are you satisfied you have the resources to do that?

Mr. GREWAL. I could always use more resources, but we are making the best of it with the additional 20 slots, and then hopefully, we'll get the 125 additional slots that we have asked for.

Mr. CASTEN. Okay. I yield back. Thank you.

Chairman SHERMAN. I should point out that votes have been called. Some 413 Members have not voted, and 7 minutes and 13 seconds are remaining on the clock. We may be able to conclude the hearing before we all have to go vote. I will announce when we are down to 110 people who haven't voted, and if we don't get to conclude, we will reconvene after the two votes.

I now recognize the gentleman from Indiana, Mr. Hollingsworth.

Mr. HOLLINGSWORTH. Director Grewal, thank you for being here today. I know you have been asked many questions, some of which are inside your bailiwick and others perhaps outside. I want to ask something that I believe is very, very germane to your daily job enforcement. Do you agree that there is a difference in the legal authority and legal obligations you have to enforce rules and regulations promulgated by the SEC as compared to guidance from staff through staff accounting bulletins?

Mr. GREWAL. Excuse me. Staff accounting bulletins are exactly that, they are guidance that the Office of the Chief Accountant (OCA) offers on an issue where there has been some question and is there—

Mr. HOLLINGSWORTH. Is there a difference in the industry? I understand the definition of staff accounting bulletin. Is there a difference in the enforcement, or level of enforcement, or the actions of enforcement, or the likelihood of enforcement of these things under your control between rules and regulations promulgated versus staff accounting bulletins?

Mr. GREWAL. Again, we wouldn't be involved in the enforcement of violations of staff accounting guidance.

Mr. HOLLINGSWORTH. For clarity, there is no enforcement that you would bring based on that which is promulgated or put forth through staff accounting bulletins alone?

Mr. GREWAL. Again, every violation is facts and circumstances. I don't know what else might be in that hypothetical situation.

Mr. HOLLINGSWORTH. It is not a hypothetical situation. I am asking. That is not a hypothetical situation. There is no example here. I am asking you to repeat exactly what you just said, "We do not enforce." This is what I heard you say, and I just want to make sure that you repeat it. We do not enforce, "violations," actions in contravention, I should say, to staff accounting bulletins. Is that what you said?

Mr. GREWAL. I said that staff accounting bulletins are guidance. We enforce violations of the Federal securities laws and the rules and regulations promulgated from those laws. Staff accounting guidance or staff accounting bulletins may intersect with another violation or may be part of a fact pattern and we—

Mr. HOLLINGSWORTH. Okay. But it alone is not law?

Mr. GREWAL. Standing alone, no.

Mr. HOLLINGSWORTH. It alone is not law, and you are enforcing the laws of this country, correct?

Mr. GREWAL. The laws, and the rules, and regulations that are promulgated from those laws.

Mr. HOLLINGSWORTH. Great. As you know, I wrote a letter to the SEC last week regarding Staff Accounting Bulletin No. 121 (SAB 121), signed by a majority of committee Republicans. That letter raised several concerns with the policy in the bulletin, the absence of a transparent process from SEC staff. Very specifically again, does SAB 121 legally require counterparties that participate in the activities included in the bulletin to adhere to the bulletin, legally require them to do so?

Mr. GREWAL. Again, it is guidance. And I don't mean to push off these questions on my other divisions, but that is the Office of the Chief Accountant that promulgated that—

Mr. HOLLINGSWORTH. I thought it was your office that enforced these things, or failed to, or does not enforce these things?

Mr. GREWAL. This staff accounting bulletin was promulgated by the Office of the Chief Accountant, so I would direct you to that office about how they are ensuring compliance or how they are pushing that out.

Mr. HOLLINGSWORTH. If someone refers to you an activity that is in contravention to SAB 121, and requests that you enforce it, what is your response to that?

Mr. GREWAL. It would depend on the facts and circumstances of what is referred to us. It would, again, depend on the facts and circumstances of what is referred.

Mr. HOLLINGSWORTH. And those facts and circumstances would be whether they violated other actual laws or whether they violated this guidance?

Mr. GREWAL. It could be part of a larger violation. I just can't engage with hypothetical—

Mr. HOLLINGSWORTH. But standing alone, you don't believe SAB 121 or other SABs promulgated our law and can be enforced by virtue of the law?

Mr. GREWAL. Again, they are guidance.

Mr. HOLLINGSWORTH. Understood. How does the SEC plan to address the implications of accounting firms that require organizations to adhere to that guidance?

Mr. GREWAL. Again, I would refer to the Office of the Chief Accountant that deals with those issues and deals with the accounting firms.

Mr. HOLLINGSWORTH. What I have heard you repeatedly say, which is very impactful, and I appreciate your candor, is that these staff accounting bulletins are not law and cannot be enforced as though they were law. This is something that continues to concern many firms that interact with our office, and many Americans who believe that is in contravention to how we create laws in this country. Staff accounting bulletins are carrying the force of law instead of going through the normal process by which we promulgate rules. I appreciate your candor about the difference between those two and the activities that you can and cannot undertake in enforcement as it relates to those two. Thank you, and I yield back my time.

Chairman SHERMAN. Thank you. I will point out that we are trying to organize a hearing to deal with accounting and auditing issues. We hope to have the Chief Accountant of the SEC, the Chair of the Financial Accounting Standards Board (FASB), and the Chair of the Public Company Accounting Oversight Board (PCAOB). Stay tuned.

I now recognize the gentleman from Wisconsin, Mr. Steil, and I believe you will be our last questioner.

Mr. STEIL. Last, but not least. Thank you for being here, Mr. Grewal. I appreciate it. We have covered a wide range of topics. I want to cover three in the limited time that I have. First question, can you tell us about any enforcement actions regarding proxy advisors that you have taken during your tenure at the SEC?

Mr. GREWAL. I'm sorry, I didn't hear the first part of your question.

Mr. STEIL. No worries. Can you tell us about any enforcement actions regarding proxy advisors that you have undertaken during your tenure at the Securities and Exchange Commission?

Mr. GREWAL. It will be a year for me next week, but I would have to go back and consult with our office on that and get back to you with that information.

Mr. STEIL. That would be terrific.

Is it your view that as proxy advisors are not a proxy solicitation under the 1934 Act, that you would need an action by Congress to further oversee proxy advisors? Do you think you have current authority to review proxy advisor firms in your current position?

Mr. GREWAL. Again, that is something for which I would refer you to our Policymaking Division, which is handling the proxy advisor rules and the changes thereto.

Mr. STEIL. Okay. I am pretty concerned with the changes that were just recently made. I think it was a mistake to strike down the Clayton proxy advisor rules not under your relevant jurisdiction. But I do think it is relevant as we think about the power that these two proxy advisors, who control roughly 97 percent of proxy advice in this country, play. I think it is a very reasonable place for the SEC to be providing substantive oversight.

Let me shift gears. I want to echo my colleague, Mr. Huizenga's, comments regarding the Division of Enforcement, that historically adopted a historically-broad understanding of what the term, "dealer" means. I listened to your answers, so I won't ask you my questions. But I just would note, and I think I echo my colleague here, that I want to caution that these broad definitions and aggressive enforcement approaches come with a real cost. Specifically, classifying everyone as a dealer could chill investment in particular in small public companies, and my concern is that it will hurt innovation and competition. I won't ask you a question, because I think it was covered previously. I know there is ongoing litigation in that space.

Let me get to my final topic here, and I know Mrs. Wagner commented on this. Mr. Grewal, I am really concerned about the SEC's climate disclosure proposal. You would be in the enforcement arm at the SEC, and American businesses are struggling in high inflation with labor costs, supply shortages, and mountains of red tape, while at that same time, the SEC seems determined to push companies to spend scarce resources on disclosure of where they have used non-material, climate change-related items.

I have two concerns. First, the proposal itself. Public companies already disclose material information to investors, and to force issuers to disclose information that may not be material comes with great costs and little benefit.

Second, and this is where your office comes in, I am concerned whether or not this rule would be difficult to implement, and would probably fail to achieve its desired effect. One of the trickiest aspects of the climate proposal concerns Scope 3 emissions, the downstream emissions impact, and the issuers that will be expected to report on this topic. Could you walk us through how your office intends to handle compliance cases related to Scope 3 emissions disclosures?

Mr. GREWAL. Again, Congressman, I will refer back to an earlier answer I gave on that specific question. It is impossible for me to talk about how we would enforce this rule, which has yet to be finalized and yet to be adopted, and we don't know yet what it will look like. I tried to explain how we have gone about dealing with these issues using our existing authorities.

Mr. STEIL. I appreciate that. Maybe, I can get a little more clarity then. Does your office have expertise in climate science?

Mr. GREWAL. As I mentioned earlier, where we need expertise for our enforcement actions, for example, a climate-related matter that we are prosecuting now in court, we have gone out and gotten that expertise in litigation.

Mr. STEIL. What would be the cost structure of that, in the case you just referenced?

Mr. GREWAL. It would be the same with any litigated enforcement action where we go out and retain experts within the rules that allow—

Mr. STEIL. There are individuals probably charging in the neighborhood of $1,000 an hour, rough estimate?

Mr. GREWAL. We could provide you that information.

Mr. STEIL. I think that would actually be helpful, because here is my concern, if we take the rules, if we assume to currently im-

plement, it would fall to your office. I think it would involve hundreds of individuals who would be required to have very specific climate expertise. We could judge whether or not they are politically motivated. It would cost thousands of dollars, not only for the SEC, but also for these companies to comply rather than allowing these companies to build jobs here in the United States of America.

I know we are out of time. Mr. Chairman, and recognizing that there are votes, I will yield back.

Chairman SHERMAN. Thank you. Some 341 of our colleagues have yet to record their votes, so it looks like we can conclude. The ranking member is recognized for 1 minute for a concluding statement.

Mr. HUIZENGA. Mr. Grewal, I am appreciative of you being here. This is too little, too late, in my opinion, and, frankly, on the too little, I would observe that neither side really got answers from you. There was a lot of, "you need to talk to somebody else, you need to talk to a different division head." It causes me to wonder how we are going to get those answers. And it is true, maybe the other side is a little more polite about it, but we need to have these answers because this is our constitutional duty as we, according to the Constitution, are the purse bearers for the U.S. Government, meaning you have to come to the House of Representatives for appropriations. And this committee works with our ESG counterparts on the Appropriations Committee to deal with the policy and the funding of it. So, we had better start getting some answers, especially when you are coming up and asking for more resources.

I do want to correct one thing on the ALJ situation. The breach happened in 2017. The SEC disclosed the breach in April of 2022, the statement. But according to The Wall Street Journal, the breach was discovered in the fall of 2020. That lack of time of being transparent, open, and honest with this committee and with the public is problematic. And my time is up.

Chairman SHERMAN. Thank you. I want to thank the witness for joining us, and enlightening us with his comments. There have been a number of comments from our colleagues about the need for a definition. No definition is more important than to define, "security," since that is what the SEC does. Congress really hasn't acted. Courts have acted with the Howey Test, which was not focused on digital assets, since it was written in the 1940s. But the fact remains that XRP, I think, clearly is a security, and we need enforcement, not only on those who issued the unregistered security, but on those who provided an exchange for it.

Likewise, it would be good to have a definition of, "ESG," but right now, companies in mutual funds put forward their own definitions of, "ESG," and promise the investors that they will follow them when they don't. That is when enforcement is called for. It is not enforcement by regulation to take a security, which clearly is a security, I believe, under the Howey Test and to enforce our rules against it. Of course, more clarity would be helpful.

My Republican colleagues have said that there is no formal rule that has been adopted on ESG. We understand that. You still need to go forward, and it is my understanding that you are going forward in those areas where they are not meeting their own stated standards.

The Chair notes that some Members may have additional questions for this witness, which they may wish to submit in writing. Without objection, the hearing record will remain open for 5 legislative days for Members to submit written questions to this witness and to place his responses in the record. Also, without objection, Members will have 5 legislative days to submit extraneous materials to the Chair for inclusion in the record.

This hearing is now adjourned.

[Whereupon, at 11:35 a.m., the hearing was adjourned.]

A P P E N D I X

July 19, 2022

Testimony on "Oversight of the SEC's Division of Enforcement"
by
Gurbir S. Grewal
Director, Division of Enforcement
United States Securities and Exchange Commission

Before the
United States House of Representatives
Committee on Financial Services
Subcommittee on Investor Protection, Entrepreneurship, and Capital Markets

July 19, 2022

Chairman Sherman, Ranking Member Huizenga, and Members of the Subcommittee:

Thank you for inviting me to testify today on behalf of the Division of Enforcement ("Enforcement" or the "Division") of the U.S. Securities and Exchange Commission ("SEC" or the "Commission").

Since its founding more than 85 years ago, the SEC has stayed true to its three-part mission of protecting investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation. Central to that mission is the work of the SEC's Division of Enforcement. The Division conducts investigations into possible violations of the federal securities laws and prosecutes the Commission's civil suits in the federal courts and in administrative proceedings. And each year, the Commission brings hundreds of civil enforcement actions and obtains meaningful relief, including disgorgement of ill-gotten gains and civil monetary penalties – which are frequently returned to harmed investors – as well as injunctions and other prophylactic relief.

During fiscal year 2021, which ended on September 30, 2021, despite the challenges presented by the global pandemic and the increasing complexity of our investigations, the SEC filed 434 new enforcement actions, representing a seven percent increase over the prior year. Seventy percent of these new or "stand-alone" actions involved at least one individual defendant or respondent.[1] In addition, the SEC's whistleblower program had a record-breaking year, with the SEC awarding a total of $564 million to 108 whistleblowers, compared to 39 whistleblowers in fiscal year 2020,[2] and surpassing $1 billion in awards over the life of the program.[3]

Since my appointment approximately one year ago, I have been amazed by the talent and unique expertise of the Division's staff of dedicated professionals in our twelve offices across the

[1] Press Release 2021-238, SEC Announces Enforcement Results for FY 2021 (Nov. 18, 2021), *available at* https://www.sec.gov/news/press-release/2021-238.
[2] *See* "SEC Division of Enforcement Publishes Annual Report for Fiscal Year 2020" (Nov. 2020), *available at* https://www.sec.gov/news/press-release/2020-274.
[3] Press Release 2021-238, SEC Announces Enforcement Results for FY 2021 (Nov. 18, 2021), *available at* https://www.sec.gov/news/press-release/2021-238.

country. They work tirelessly day in and day out to hold those who violate our securities laws accountable, return money to harmed investors, and protect the fairness and competitiveness of our capital markets. Yet, many Americans' trust in our financial markets and institutions is at near historic lows.[4] While there is no single cause for this decline, repeated lapses by large businesses, gatekeepers, and other market participants, coupled with the perception that we – the regulators – are failing to hold them appropriately accountable have contributed to this decline. And, some believe that there are two sets of rules: one for the big and powerful and another for everyone else. As a result, one of my goals as Director is to help restore the public's trust in our financial markets and institutions and to make clear that there is only one set of rules. The Division aims to enhance Americans' trust through robust enforcement, robust remedies, and robust compliance.

ENFORCEMENT PRIORITIES

Robust Enforcement

Robust enforcement requires the Division to be the cop on the beat and cover the entire securities waterfront, investigating and litigating every type of case within our remit with a sense of urgency. It also requires us to keep pace with new areas of importance for investors, as well as the continually evolving risks facing investors and the markets. For example, the Division is taking proactive steps to police areas such as crypto assets and cybersecurity and brought a number of first-of-their-kind enforcement actions over the past calendar year.[5]

The SEC also recently announced the allocation of 20 additional positions to our Crypto Assets and Cyber Unit.[6] Since its creation in 2017, the unit has brought more than 80 enforcement actions related to fraudulent and unregistered crypto asset offerings and platforms, resulting in monetary relief totaling more than $2 billion, as well as numerous actions against SEC registrants and public companies for failing to maintain adequate cybersecurity controls and appropriately disclose cyber-related risks and incidents. The expanded unit will leverage the agency's expertise to ensure investors are protected in the crypto markets and from cyber-related threats, with a focus on investigating securities law violations related to crypto asset offerings,

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[4] *See* "Americans' Confidence in Major U.S. Institutions Dips" (July 14, 2021), *available at* https://news.gallup.com/poll/352316/americans-confidence-major-institutions-dips.aspx (finding that, in 2021, 33% of respondents have "a great deal" or "quite a lot" of confidence in banks; 29% in technology companies; and 18% in big business); "Confidence in Institutions," *available at* https://news.gallup.com/poll/1597/confidence-institutions.aspx.

[5] *See, e.g.,* Press Release 2022-110, SEC Charges Firm and Five Brokers with Violations of Reg BI (June 16, 2022), *available at* https://www.sec.gov/news/press-release/2022-110; Press Release 2022-70, SEC Charges Archegos and its Founder with Massive Market Manipulation Scheme (Apr. 27, 2022), *available at* https://www.sec.gov/news/press-release/2022-70; Press Release 2022-26, BlockFi Agrees to Pay $100 Million in Penalties and Pursue Registration of its Crypto Lending Product (Feb. 14, 2022) (settled), *available at* https://www.sec.gov/news/press-release/2022-26; Press Release 2021-176, SEC Charges App Annie and its Founder with Securities Fraud (Sept. 14, 2021) (settled), *available at* https://www.sec.gov/news/press-release/2021-176.

[6] Press Release 2022-78, SEC Nearly Doubles Size of Enforcement's Crypto Assets and Cyber Unit (May 3, 2022), *available at* https://www.sec.gov/news/press-release/2022-78.

exchanges, broker-dealers, and lending and staking products; decentralized finance ("DeFi") platforms; non-fungible tokens ("NFTs"); and stablecoins.

Robust enforcement also includes a focus on gatekeeper accountability. Gatekeepers, such as accountants and attorneys, are often the first lines of defense against misconduct. When they fail to live up to their obligations, investors and the integrity of our markets suffer. The SEC has brought enforcement actions against gatekeepers who engaged in wrongdoing themselves or attempted to cover up wrongdoing, engaged in conduct that crossed a clear line, or failed meaningfully to implement compliance programs, policies and procedures for which the gatekeeper had direct responsibility. For example, the SEC recently charged Ernst & Young LLP ("EY") in connection with cheating by a significant number of its audit professionals on exams required to obtain and maintain Certified Public Accountant ("CPA") licenses, and for withholding evidence of this misconduct from the Division during our investigation of the matter. EY admitted the facts underlying the SEC's charges and agreed to pay a $100 million penalty and to undertake extensive remedial measures to fix the firm's ethical issues.[7] We will continue to take a hard look at gatekeepers to ensure that they are fulfilling their own professional responsibilities and not giving cover to corporations or executives engaged in possible misconduct.

Robust Remedies

Restoring trust in our financial markets and institutions also requires the use of robust remedies. In addition to punishing wrongdoers for violations of the securities laws, our remedies must deter those violations from happening in the first place. They must be viewed as more than the cost of doing business. The public must have confidence in knowing that financial institutions and other market participants are being held accountable by regulators such as the SEC when they are not playing by the rules.

The factors that guide our penalty recommendations are no secret – we assess the conduct at issue, in light of the statutory tier factors and judicial opinions, and look to comparable cases. In arriving at our recommendations to the Commission, we are assessing whether penalties in prior comparable cases have been sufficient to appropriately deter the misconduct at issue. Where they have not been, we will seek stiffer penalties, both in settlement negotiations and, if necessary, in litigation. We are also seeking heightened penalties for recidivists because prior penalties clearly have not had the appropriate deterrent effect.

In addition, prophylactic relief – such as officer and director bars, associational bars, suspensions, conduct-based injunctions, and undertakings – is an important part of robust remedies. Such relief directly protects investors and market integrity by preventing a violator of the securities laws from engaging in future misconduct and occupying a core gatekeeper role in the securities markets. These tools also enhance the public's trust that all financial institutions

[7] Press Release 2022-114, Ernst & Young to Pay $100 Million Penalty for Employees Cheating on CPA Ethics Exams and Misleading Investigation (June 28, 2022) (settled), *available at* https://www.sec.gov/news/press-release/2022-114.

and market participants are playing by the same rule set. We take an especially hard look at whether we need to deploy prophylactic tools if the specific offender is a recidivist.

Although we will continue to recommend no-admit-no-deny settlements in the majority of cases, we will seek admissions from wrongdoers in appropriate cases, where heightened accountability and acceptance of responsibility are in the public interest.[8] When it comes to accountability, few things rival the magnitude of wrongdoers admitting that they broke the law. Admissions also give greater clarity regarding the facts of the violations and send a strong deterrent message to other market participants and are, therefore, important to building public trust.

Robust Compliance

Finally, robust compliance is critical to restoring trust. Robust compliance is a responsibility shared by all market participants. We are in a time of rapid and profound technological change. While this has the potential to amplify the dynamism of our markets and increase access and transparency for our investors, it also creates new avenues for misconduct. Public companies and other market participants therefore need to think rigorously about how their specific business models and products interact with both emerging risks and their obligations under the federal securities laws, and tailor their internal controls and compliance practices and policies accordingly. In other words, they cannot rely on check-the-box compliance policies, but should consider, where appropriate, developing bespoke policies tailored to their businesses and the associated risks. Where they fall short, we have not hesitated in holding them accountable.[9]

Firms also need to respond appropriately to red flags and make timely and accurate required disclosures, which are essential to investor protection and enhancing trust and confidence in the markets. And, gatekeepers must foster a proactive culture of compliance and responsibility – both for themselves and for their clients. The Division will vigorously enforce the securities laws and rules that go to the heart of robust compliance, including those concerning required disclosures, misuse of nonpublic information, cybersecurity, and the violation of record-keeping obligations.[10]

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[8] *See, e.g.*, Press Release 2022-84, SEC Charges Allianz Global Investors and Three Former Senior Portfolio Managers with Multibillion Dollar Securities Fraud (May 17, 2022) (settled as to Allianz Global Investors and litigating against three former senior portfolio managers), *available at* https://www.sec.gov/news/press-release/2022-84; Press Release 2021-262, JPMorgan Admits to Widespread Recordkeeping Failures and Agrees to Pay $125 Million Penalty to Resolve SEC Charges (Dec. 17, 2021) (settled), *available at* https://www.sec.gov/news/press-release/2021-262.

[9] *See, e.g.*, Press Release 2021-241, McKinsey Affiliate to Pay $18 Million for Compliance Failures in Handling of Nonpublic Information (Nov. 19, 2021) (settled), *available at* https://www.sec.gov/news/press-release/2021-241; Press Release 2022-114, Ernst & Young to Pay $100 Million Penalty for Employees Cheating on CPA Ethics Exams and Misleading Investigation (June 28, 2022) (settled), *available at* https://www.sec.gov/news/press-release/2022-114.

[10] *See, e.g.*, 15 U.S.C. § 80b-4a; 15 U.S.C. § 78q(a).

FY 2023 BUDGET REQUEST

Despite the successes and priorities outlined above, the number of Enforcement employees has decreased over time. The Division faces significant and mounting challenges, as described in more detail in the FY 2023 budget request that the SEC submitted to Congress earlier this year.[11] Some of the challenges are obvious, such as the broad spectrum of securities law violations that occur across the United States each year and the unexpected and unprecedented market events such as the global pandemic, market volatility in early 2021, and more recent volatility across crypto assets and offerings that require significant Enforcement resources.

But, others are less obvious, though still highly meaningful, such as the significant growth of the financial markets and the increasing sophistication of securities products and market structure. For example, in the past five years, the number of registered entities has grown by 12 percent (from 26,000 to 29,000).[12] The volatile and speculative crypto marketplace has attracted tens of millions of American investors and traders.[13] Moreover, many of our investigations are becoming more difficult as fraudsters find new ways to communicate that require us to review ever-broader sources of evidence. To protect investors and the markets, we must continuously evolve and adapt as wrongdoers and products, particularly in new and emerging areas – like the crypto markets – become increasingly sophisticated and the related misconduct becomes harder to detect and increasingly complex and international in nature.

Internally, the Division is also required to analyze a massive volume of data each year, including, for example, approximately 46,000 tips, complaints, and referrals from, among others, members of the public during fiscal year 2021.[14] At any given time, the Division has approximately 1,500 open investigations.[15] The Division also handles an expansive docket of difficult and complex litigation and trials, often against well-funded adversaries. We have seen an uptick in the number of cases that are litigating and going to trial, and during fiscal year 2021, the Division had approximately 2,000 pending civil litigations and 1,200 pending administrative proceedings.[16]

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[11] *See* "Fiscal Year 2023 *Congressional* Budget Justification, Annual Performance Plan; Fiscal Year 2021 Annual Performance Report" (p. 25), *available at* https://www.sec.gov/files/FY%202023%20Congressional%20Budget%20Justification%20Annual%20Performance%20Plan_FINAL.pdf.

[12] *See* Testimony at Hearing before the Subcommittee on Financial Services and General Government U.S. House Appropriations Committee (May 17, 2022), *available at* https://www.sec.gov/news/testimony/gensler-testimony-fsgg-subcommittee#_ftn3.

[13] *See* Testimony at Hearing before the Subcommittee on Financial Services and General Government U.S. House Appropriations Committee (May 17, 2022), *available at* https://www.sec.gov/news/testimony/gensler-testimony-fsgg-subcommittee#_ftn3 (citing Andrew Perrin/Pew Research Center, "16% of Americans say they have ever invested in, traded or used cryptocurrency" (Nov. 11, 2021), *available at* https://www.pewresearch.org/fact-tank/2021/11/11/16-of-americans-say-they-have-ever-invested-in-traded-or-used-cryptocurrency/).

[14] *See* "Fiscal Year 2023 *Congressional* Budget Justification, Annual Performance Plan; Fiscal Year 2021 Annual Performance Report" (p. 25), *available at* https://www.sec.gov/files/FY%202023%20Congressional%20Budget%20Justification%20Annual%20Performance%20Plan_FINAL.pdf.

[15] *See id.*

[16] *See id.*

These challenges require the Division to constantly assess and re-assess how best to allocate the Division's limited resources in the most effective manner to address the most significant and pressing risks facing investors and the financial markets. The SEC's FY 2023 budget seeks additional staff to enable Enforcement to meet these mounting challenges and to maintain an effective investigative capacity and deterrent presence for the benefit of our markets and investors.

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Through robust enforcement, robust remedies, and robust compliance, we will aim to do our part in restoring public trust in our financial markets and institutions. Thank you for inviting me here today to discuss the Division of Enforcement. I am happy to answer any questions you may have.

Representative Auchincloss
Questions for the Record
Subcommittee on Investor Protection, Entrepreneurship, and Capital Market
Oversight of the SEC's Division of Enforcement
July 19, 2022

Gurbir S. Grewal, Division of Enforcement, Securities and Exchange Commission Director

1. Industry participants have a responsibility to follow the rules and regulations determined by the SEC. However, participants in emerging technologies may not know their actions fall under SEC jurisdiction.

   Do you have a process to educate participants in emerging industries regarding their responsibilities under SEC regulations? If so, can you provide details of the Agency's process?

The SEC and its staff seek to establish a regulatory environment for investors and market participants that fosters innovation, investor protection, market integrity, and ultimately confidence. One key component of these efforts is engagement with market participants to educate them on their obligations under the federal securities laws.

For example, the SEC established the FinHub in October 2018 to lead engagement efforts with the FinTech community. That engagement has included providing guidance and clarity to market participants, including through the April 2019 framework for analyzing whether a crypto asset is offered and sold as an investment contract, and therefore, is a security. The FinHub staff continues to conduct outreach in a number of ways, including by hosting peer-to-peer meetings to engage with FinTech communities in a number of FinTech areas, including distributed ledger technology and crypto assets.

Staff across the Commission's other Divisions and Offices have similarly published guidance and otherwise informed the market regarding emerging technologies. In particular, the SEC's Office of Investor Education and Advocacy often publishes investor alerts and bulletins, a number of which address emerging technologies and attendant risks they pose to investors.

Specifically with respect to Enforcement, the Commission issues litigation releases concerning all civil lawsuits brought by the Commission in federal court and links to notices and orders concerning the institution and/or settlement of administrative proceedings. From time to time, the Commission also authorizes the issuance of a Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934. In 2017, the Commission issued a 21(a) report concerning "The DAO," which cautioned market participants that offers and sales of digital assets by "virtual" organizations are subject to the requirements of the federal securities laws. In an accompanying press release, the SEC noted that whether a particular investment transaction involves the offer or sale of a security will depend on the facts and circumstances, including the economic realities of the transaction. Enforcement staff and leaders also frequently participate

in speaking engagement and investor outreach events designed to educate investors and other market participants.

2. Industry participants have expressed concern that the SEC is relying on enforcement actions, rather than rulemaking to educate other industry participants.

   Do you believe that enforcement actions are more productive when there is consistent and clear rulemaking?

The SEC enforces existing federal securities laws, as well as the rules and regulations promulgated pursuant to those laws. Rulemaking is not a substitute for the enforcement of Securities laws and enforcement actions are not less effective in the absence of rulemaking. Our application of those laws, rules, and regulations is governed by decades of well-developed case law. The resiliency of these laws is reflected by how long they have stood the test of time as capital markets have continued to evolve. And the fact that we continue to see innovation and capital formation in our markets demonstrates that these laws and regulations have struck the right balance in both protecting investors and facilitating growth and new ideas.

Rep. Emmer: Question for the Record
Subcommittee on Investor Protection and Capital Markets
Hearing entitled "Oversight of the SEC's Division of Enforcement"

1. Question for Mr. Grewal: Some statements have been made at the hearing suggesting that it is a settled question regarding whether XRP is a security. Do you agree that the filing of the lawsuit is not a determination and there is, in fact, ongoing litigation that will decide this question?

The litigation in this matter, in which the SEC alleged that the Defendants engaged in unregistered offers and sales of XRP is ongoing. The SEC recently filed its summary judgment motion in court.

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