

“GRADE INCOMPLETE”: EXAMINING THE SECURITIES AND EXCHANGE COMMISSION’S ATTEMPT TO IMPLEMENT CREDIT RATING AND CERTAIN CORPORATE GOVERNANCE REFORMS OF DODD-FRANK

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ABSTRACT

Following the financial crisis of 2007-2009, Congress passed the Dodd-Frank Act with stated goals, among others, of creating a sound economic foundation and protecting consumers. The Dodd-Frank Act creates several new agencies and restructures the financial regulatory system, yet controversies remain on the promulgation of new rules and the overall effectiveness in accomplishing the stated goals of the Act.

This Article briefly discusses the status of rulemaking by newly created agencies and the restructured financial regulatory system mandated by the Dodd-Frank Act three years after its passage. Next, we focus on certain aspects of the SEC and its charge from Dodd-Frank to implement new agencies and regulations. Specifically, we examine the SEC efforts to establish the Office of Credit Ratings and its regulations and the SEC’s efforts related to additional executive compensation disclosure regulations required by Dodd-Frank.

INTRODUCTION

Following the financial crisis of 2007-2009, Congress adopted the Dodd-Frank Wall Street Reform and Consumer Protection Act (“Dodd-Frank”),¹ a broadly-sweeping statute which increased regulatory influence on a large part of the U.S. economy. Congress passed Dodd-Frank with stated goals, among others, of creating a sound economic foundation and protecting consumers.² Dodd-Frank created several new agencies and restructured the financial regulatory system,³ yet controversies remain on the promulgation of new rules and the overall effectiveness in accomplishing the goals of the Act. According to Paul Hastings, as of the third anniversary of Dodd-Frank on July 21, 2013, “only 40% of the

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1. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

2. S. COMM. ON BANKING, 111TH CONG., BRIEF SUMMARY ON THE DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT 1, *available at* http://www.banking.senate.gov/public/_files/070110_Dodd_Frank_Wall_Street_Reform_comprehensive_summary_Final.pdf.

3. *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

approximately 400 required rules have been finalized.”⁴ On its website, the U.S. Securities and Exchange Commission (the “SEC”) reports that Dodd-Frank “contains more than 90 provisions that require SEC rulemaking, and dozens of other provisions that give the SEC discretionary rulemaking authority.”⁵ In addition, the SEC claims that it proposed or adopted rules for more than 75% of the required provisions as of February 2014.⁶ New regulations from the various entities are being proposed and adopted on a weekly basis, yet additional complications occur from both legislative actions to unwind parts of Dodd-Frank and court rulings discarding adopted or proposed regulations.⁷

The Dodd-Frank Act reorganized the U.S. Federal regulatory system of banking, finance, and securities to “strengthen oversight of insured depository institutions and nonbank financial companies”⁸ and to establish a more efficient implementation of consumer protection system by consolidating responsibilities “that had been fragmented across multiple agencies.”⁹ Eleven federal agencies received new funding as part of the implementation of the Dodd-Frank Act. In addition, Dodd-Frank consolidated and reorganized the regulatory oversight of depository and nonbank financial companies through new offices or sections with three federal agencies: the Federal Reserve, the Department of the Treasury (the “Treasury”), and the SEC. Restructured or newly created agencies within the Federal Reserve and the Treasury include the Consumer Financial Protection Bureau (CFPB), an independent bureau within the Federal Reserve System, and three independent offices within the Treasury: the Office of Financial Research (OFR), the Financial Stability Oversight Council (FSOC), and the Federal Insurance Office (FIO). Dodd-Frank also abolished an office within the Treasury, the Office of Thrift Supervision (OTS). It merged OTS’s responsibilities to regulate federally chartered and state chartered banks and savings and loan associations into the Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance Corporation (FDIC), the Federal Reserve, and the

4. THE PAUL HASTINGS GLOBAL BANKING AND PAYMENT SYSTEMS GROUP, DODD-FRANK ACT THREE YEARS LATER . . . STILL A WORK IN PROGRESS 1 (2013), available at <http://www.paulhastings.com/Resources/Upload/Publications/StayCurrent-Dodd-Frank-Act-Still-a-Work-in-Progress.pdf>.

5. *Implementing the Dodd-Frank Wall Street Reform and Consumer Protection Act*, U.S. SEC. & EXCH. COMM’N, <http://www.sec.gov/spotlight/dodd-frank.shtml> (last modified Feb. 13, 2014).

6. *Id.*

7. See, e.g., Jill E. Fisch, *The Long Road Back: Business Roundtable and the Future of SEC Rulemaking*, 36 SEATTLE U. L. REV. 695 (2013); Paul Rose & Christopher J. Walker, *Dodd-Frank Regulators, Cost-Benefit Analysis, and Agency Capture*, 66 STAN. L. REV. ONLINE 9 (2013), available at <http://www.stanfordlawreview.org/sites/default/files/online/articles/DoddFrankFinal.pdf> (discussing so-called “proxy access” rule and the subsequent legal response).

8. U.S. Gov’t Accountability Office, GAO-11-808T, *Dodd-Frank Act: Eleven Agencies’ Estimates of Resources for Implementing Regulatory Reform 1* (2011), available at www.gao.gov/assets/90/82449.pdf.

9. *Id.*

CFPB.

This Article focuses on the impact of Dodd-Frank on the SEC more than three years after its passage and its increased and expanded role in the regulatory rulemaking process. Specifically, it provides a brief review and status of rulemaking and restructuring mandated by Dodd-Frank and then in greater detail analyzes: 1) the SEC’s role in establishing the Office of Credit Ratings (OCR) and the accompanying regulatory structure designed to provide oversight to the rating agencies; and 2) the SEC’s role in proposing and adopting regulations mandated by Dodd-Frank that intended to enhance disclosure of executive compensation to shareholders and other stakeholders. In the first case, Dodd-Frank affects a segment of the financial services sector by attempting to address problems with the economic model of the credit rating agencies and flawed incentives that resulted in ratings that did not appear to appropriately account for credit risk and have been blamed for exacerbating the financial crisis.¹⁰ In the latter case, however, the corporate governance regulations adopted by the SEC affect all publicly-traded companies.¹¹ Therefore, the reach of Dodd-Frank and the costs it imposes on firms extends well beyond the financial sector. The Article will conclude with a discussion of the challenges ahead for the SEC related to its role in implementing Dodd-Frank.

I. RESTRUCTURING WITHIN THE SEC

Dodd-Frank required new offices within the SEC, which the Office of Investor Education and Advocacy (OIEA), the Office of Municipal Securities, the Office of Credit Ratings (OCR), and the Office of Whistleblower Protection.¹² Each office has autonomy from general overview of the SEC.

A. Office of Investor Education and Advocacy

The OIEA assists investors by functioning as a liaison between investors and the SEC.¹³ It represents the interest of investors by providing feedback on proposed SEC rules and regulations, promoting regulations and rules that benefit investors, and analyzing investor problems with certain financial services and products.¹⁴

10. THE PRESIDENT’S WORKING GROUP ON FINANCIAL MARKETS, PROGRESS UPDATE ON MARCH POLICY STATEMENT ON FINANCIAL MARKET DEVELOPMENTS 2 (2008), available at <http://www.treasury.gov/resource-center/fin-mkts/Documents/q4progress%20update.pdf>.

11. *The Investor’s Advocate: How the SEC Protects Investors, Maintains Market Integrity, and Facilitates Capital Formation*, U.S. SEC. & EXCH. COMM’N, <http://www.sec.gov/about/whatwedo.shtml> (last modified Jun. 10, 2013).

12. *Testimony on Oversight of the SEC: Hearing Before the H. Comm. on Fin. Services*, 113th Cong. (2013) (statement of Mary Jo White, Chair, U.S. Sec. & Exch. Comm’n).

13. See *The Investor’s Advocate: How the SEC Protects Investors, Maintains Market Integrity, and Facilitates Capital Formation*, U.S. SEC. & EXCH. COMM’N, available at <http://www.sec.gov/about/whatwedo.shtml#org>.

14. 15 U.S.C. § 78d(g)(4) (2011).

B. Office of Municipal Securities

The Office of Municipal Securities (OMS) establishes policies and administers rules to regulate the practices of municipal securities brokers and dealers, municipal securities advisors, municipal securities investors, and municipal securities issuers.¹⁵ OMS works with the Municipal Securities Rulemaking Board (MSRB).¹⁶ The MSRB is a self-regulated organization created by Congress in 1975 to create rules for the municipal securities market that protect investors, the public interest, and state and local government issuers; provide equal regulation of municipal securities dealers; establish guidelines for the dissemination of market information; and promote market leadership, outreach and education.¹⁷ The OMS is the office within the SEC that enforces the MSRB rules.¹⁸ In July 2012, OMS issued a comprehensive report with recommendations to improve the structure of the municipal securities market and to enhance disclosure to investors.¹⁹

C. Office of Credit Ratings

OCR is responsible for improving the accuracy of the credit rating agencies and the creation of procedures and processes to provide stability and control of the credit rating system.²⁰ The 2008 financial crisis put into question the ability of nationally recognized statistical rating organizations (NRSROs) to produce accurate credit ratings on debt securities.²¹ This accuracy issue materialized at that time due to the widespread default of collateralized debt obligations and other asset-backed securities, including bundled subprime residential loan mortgages.²² Congress believed that the inaccuracies of the credit rating system

15. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 979, 124 Stat. 1376, 1926 (2010).

16. See *Office of Municipal Securities*, U.S. SEC. & EXCH. COMM'N, available at http://www.sec.gov/municipal#U3TQMrfD_cs.

17. See generally MUNICIPAL SECURITIES RULEMAKING BOARD, <http://www.msrb.org/> (last visited May 15, 2014).

18. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 979, 124 Stat. 1376, 1926 (2010).

19. U.S. SEC. & EXCH. COMM'N, REPORT ON MUNICIPAL SECURITIES MARKET (2012), available at <http://www.sec.gov/news/studies/2012/munireport073112.pdf>.

20. See *The Investor's Advocate: How the SEC Protects Investors, Maintains Market Integrity, and Facilitates Capital Formation*, U.S. SEC. & EXCH. COMM'N, www.sec.gov/about/whatwedo.shtml#org.

21. See JOSEPH R. MASON & JOSHUA ROSNER, WHERE DID THE RISK GO? HOW MISAPPLIED BOND RATINGS CAUSE MORTGAGE BACKED SECURITIES AND COLLATERALIZED DEBT OBLIGATION MARKET DISRUPTIONS 34-51 (2007), available at www.researchgate.net/.../32bfe5126a481bed33.pdf.

22. See generally Claire A. Hill, *Why Did Rating Agencies Do Such a Bad Job Rating Subprime Securities?*, 71 U. PITT. L. REV. 585 (2010) (describing the process of NRSROs rating the credit worthiness of subprime securities).

were a key element of the cause of the 2008 financial crisis.²³ Prior to the crisis, NRSROs were subject to oversight by the SEC through the Credit Rating Agency Reform Act.²⁴ However, the SEC’s oversight was limited to establishing guidelines for the qualification of credit rating agencies as NRSROs, the regulation of the internal processes regarding record keeping, and the prevention of conflict of interests of NRSROs and the securities they rated.²⁵ The SEC was prohibited from having authority to regulate the credit rating methodologies of NRSROs.

Dodd-Frank attempted to address the accuracy of the NRSRO rating system by enhancing the authority of the SEC over NRSROs.²⁶ The powers of the SEC over the credit rating system were consolidated into the OCR, an independent office within the SEC.²⁷ The primary purpose of the OCR is to enhance the regulation, accountability, and transparency of NRSROs.²⁸ The OCR is charged with administering the rules of the SEC to encourage more competition for three of the largest NRSROs: Moody’s Investor Service (Moody’s),²⁹ Standard & Poor’s (S&P),³⁰ and Fitch Ratings (Fitch).³¹ The OCR also provides transparency of NRSROs to ensure credit ratings are not unduly influenced by conflicts of interest and ensures that firms provide greater disclosure to investors.³² Dodd-Frank requires, without SEC rulemaking, that the OCR conducts annual reviews of each NRSRO and produces a public report assessing compliance with federal

23. See 156 CONG. REC. S3977-79 (daily ed. May 19, 2010) (statement of Senator Christopher Dodd agreeing with other members of Congress that the erroneous credit ratings of asset-backed securities had a central role in the financial crisis).

24. Credit Rating Agency Reform Act of 2006, Pub. L. No. 109-291, § 4(a), 120 Stat. 1327 (2006).

25. *Id.*

26. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 931, 124 Stat. 1376, 1872 (2013).

27. *Id.* §§ 931-939H.

28. See *About the Office of Credit Ratings*, SEC. & EXCH. COMM’N, <http://www.sec.gov/about/offices/ocr.shtml> (last visited May 15, 2014).

29. The predecessor of Moody’s Investor Services was founded in 1900, and in 1909 began analysis of the stocks and bonds of America’s railroads. See *Moody’s History: A Century of Markey Leadership*, MOODY’S CORPORATION, <http://v3.moody.com/Pages/atc001.aspx> (providing the history of Moody’s Investor Services) (last visited May 15, 2014).

30. Standard & Poor’s was created in 1868, providing a financial manual on America’s railroads. See *A Short History of Standard & Poor’s: Q & A*, TELEGRAPH, <http://www.telegraph.co.uk/finance/financialcrisis/8937653/A-short-history-of-Standard-and-Poors-QandA.html> (providing a brief history of Standard & Poor’s) (last visited May 15, 2014).

31. Fitch Ratings was founded in 1913. See *About Us*, FITCH RATINGS, <https://www.fitchratings.com/web/en/dynamic/about-us/about-us.jsp> (providing the history of Fitch Ratings) (last visited May 15, 2014).

32. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 942, 124 Stat. 1376, 1896-97 (2010).

securities laws and SEC rules.³³ Each NRSRO is required to establish a board of directors, the majority of which is comprised of independent directors, to create more accountability.³⁴ Additional rules require disclosure of conflicts of interest with respect to sales and marketing practices, review of transactions involving former credit analysts that leave NRSROs, and assessment of fines and penalties on non-compliance by NRSROs.³⁵ The OCR's ability to require disclosure on credit rating methodologies of NRSROs is key to its authority.³⁶

Recent litigation questions whether the SEC rules resulting from the 2006 Credit Agency Reform Act³⁷ have increased credit rating competition among NRSROs by reducing the control of the three largest NRSROs or created alternative methods of evaluating complex securities.³⁸ On February 4, 2013, the Department of Justice filed a lawsuit against S&P, and its parent company, McGraw-Hill Companies, Inc.³⁹ The lawsuit alleges S&P knowingly issued inflated credit ratings for certain collateralized debt obligations in 2006.⁴⁰ On July 8, 2013, during the first court hearing on the lawsuit, S&P countered the lawsuit with a motion to dismiss the case on grounds that reasonable investors would not rely on its generic statements about the credit rating systems.⁴¹ The U.S. District Court for the Central District of California Southern Division Judge David O. Carter, denied S&P's motion to dismiss, questioning S&P's claim that

33. *Id.* § 943.

34. *Id.* § 932(t).

35. *Id.* §§ 932(q), (s).

36. *Id.* § 932(p); *see also* U.S. SEC. & EXCH. COMM'N, OFFICE OF CREDIT RATINGS, <http://www.sec.gov/about/offices/ocr.shtml> (last visited May 15, 2014).

37. Credit Rating Agency Reform Act of 2006, 109 P.L. 291, 120 Stat. 1327 (The Act was enacted September 29, 2006 to improve credit rating quality to protect investors and increase competition for credit rating by reducing the influence of the big 3 NRSROs—S&P, Moody's, and Fitch—changing the NRSRO designation process to allow smaller credit rating companies to qualify as NRSROs).

38. *See* Daniel Fisher, *Suing S&P Won't Cure The Problem of Relying On Rating Agencies*, FORBES (Feb. 4, 2013, 4:09 PM), <http://www.forbes.com/sites/danielfisher/2013/02/04/suing-sp-wont-cure-the-problem-of-relying-on-ratings-agencies/> (claiming the lawsuit will not resolve the conflict of interest between rating agencies and securities issuers.); Matt Robinson, *S&P Lawsuit Undermined by SEC Rules That Impede Competition*, BLOOMBERG (Feb. 6, 2013, 11:47 AM), <http://www.bloomberg.com/news/2013-02-06/s-p-lawsuit-undermined-by-sec-rules-impeding-ratings-competition.html>. (describing the lack of significant changes in the influence of the big 3 NRSROs—S&P, Moody's, and Fitch—and in the methodology of rating complex securities, after the implementation of new SEC rules resulting from Credit Rating Agency Reform Act).

39. United States District Court for the Central District of California, Southern Division, Filed Case No.: CV 13-0779 DOC (JCGx). *See* Department of Justice Complaint, <http://www.ustice.gov/iso/opa/resources/849201325104924250796.PDF>

40. *Id.*

41. Edvard Pettersson, *S&P Raises Puffery Defense Against U.S. Ratings Case*, BLOOMBERG (July 8, 2013, 4:15 PM), <http://www.bloomberg.com/news/2013-07-08/s-p-to-argue-puffery-defense-n-first-courtroom-test.html>.

its statements were not relied on by investors.⁴² Since the court’s decision on the motion to dismiss, there have been several status hearings on the progress of the suit and on April 14, 2014, the court ruled on motions by the defendant to split the suit into phases and to compel discovery and the plaintiff’s cross motion to strike defendant’s First Amendment retaliation defense.⁴³ The court denied the defendant’s phased trial motion, partially granted the defendant’s motion to compel discovery and denied the plaintiff’s cross motion to strike defense.⁴⁴

D. Enforcement and the Office of the Whistleblower

In addition to the extra regulatory framework for the SEC, Dodd-Frank also attempted to assist enforcement efforts with its mandate of the creation of the Office of the Whistleblower.⁴⁵ With a goal of encouraging individuals to report securities fraud and abuses within the financial markets, the Office of the Whistleblower provides monetary rewards to individuals who report information to the SEC that leads to SEC enforcement action resulting in sanctions over \$1 million.⁴⁶ The range for awards is between 10% and 30% of the money collected.⁴⁷ Under Dodd-Frank, the Office of the Whistleblower also must report its activities to Congress annually, including the number of complaints and the number and magnitude of awards granted.⁴⁸

According to the Fiscal Year 2013 Annual Report on the Dodd-Frank Whistleblower Program, the Office of the Whistleblower received just over 3,000 “Tips, Complaints, and Referrals” in its system during the 2012 Fiscal year, and 3,238 in the 2013 Fiscal year.⁴⁹ While only one payout of \$50,000 occurred during 2012,⁵⁰ three additional payouts occurred in 2013, including an award of over \$14 million announced on October 1.⁵¹ In an SEC Press Release announcing the award, SEC Chair Mary Jo White stated, “Our whistleblower program already

42. Order Denying Defense’s Motion to Dismiss, *U.S. v. McGraw Hill Co. et. al.*, CV 13-0779 (C.D. of Cal. S. Div. July 16, 2013), *available at* <http://ia601505.us.archive.org/10/items/gov.scourts.cacd.553856/gov.uscourts.cacd.553856.34.0.pdf>. Oral arguments on the motion to dismiss were held on July 8, 2013.

43. *United States v. McGraw-Hill Cos.*, 2014 U.S. Dist. LEXIS 59408 (C.D. Cal. Apr. 15, 2014)

44. *Id.*

45. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 922, 124 Stat. 1376, 1841-49 (2010).

46. *Id.*

47. *Id.*

48. *Id.* § 924(d).

49. U.S. SEC. & EXCH. COMM’N, ANNUAL REPORT ON THE DODD-FRANK WHISTLEBLOWER PROGRAM 1 (2013), *available at* <http://www.sec.gov/about/offices/owb/annual-report-2013.pdf>.

50. *Id.* at 8.

51. *Id.* at 15; *see also* Michael Calia, *Whistleblower Awarded More than \$14 Million*, WALL STREET JOURNAL (Oct. 1, 2013, 2:52 PM), *available at* <http://online.wsj.com/news/articles/B10001424052702303918804579109530867318834>.

has had a big impact on our investigations by providing us with high quality, meaningful tips . . . [w]e hope an award like this encourages more individuals with information to come forward.”⁵²

The success of the overall enforcement program of the SEC related to the financial crisis has been subject to debate. As of December 12, 2013, the SEC indicated on its website its enforcement efforts to address “Misconduct that Led to or Arose From the Financial Crisis” had led to charges against 169 entities and individuals with total penalties, disgorgement, and other monetary relief of \$3.02 Billion.⁵³ While the amounts may seem significant, the SEC has also received criticism for its reliance on no-admit settlements in many of these cases.⁵⁴ Apparently, due to this criticism, the SEC announced in the summer of 2013 that it would review its no-admit policy and be more active in requiring firms to accept responsibility, which will also impact the SEC enforcement efforts in the future.⁵⁵

Going forward, the deterrent impact from reducing the number of no-admit settlements and the incentives to whistleblowers will become more evident.⁵⁶ Research by Professors Adam Pritchard of the University of Michigan Law School and Stephen Choi of New York University School of Law suggests that private enforcement of securities law violations through class actions may provide greater deterrence effects on firm behavior than SEC actions alone, and therefore this change in the settlement strategy of the SEC will likely impact the dynamic in private and public enforcement actions.⁵⁷ At the very least, observers should expect even more rewards as investigations prompted by these reports work through the investigative process and result in civil penalties against both individuals and firms.⁵⁸

52. Press Release, U.S. Sec. & Exch. Comm’n, SEC Awards More Than \$14 Million to Whistleblower (Oct. 1, 2013), <http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370539854258#UIW7bRATW3p>.

53. *SEC Enforcement Actions: Addressing Misconduct That Led to or Arose from the Financial Crisis*, U.S. SEC. & EXCH. COMM’N (Dec. 12, 2013), <http://www.sec.gov/spotlight/enf-actions-fc.shtml>.

54. See Edward Wyatt, *S.E.C. Changes Policy on Firms’ Admission of Guilt*, N.Y. TIMES, Jan. 6, 2012, http://www.nytimes.com/2012/01/07/business/sec-to-change-policy-on-companies-admission-of-guilt.html?_r=0 (discussing criticism leading to the eventual no-admit policy change).

55. Andrew Ackerman, *SEC Aims to Get Tougher on Fraud*, WALL ST. J. (Sept. 27, 2013, 5:50 PM), <http://online.wsj.com/news/articles/SB10001424052702304526204579099092933019908>.

56. Stephen J. Choi & Adam C. Pritchard, *SEC Investigations and Securities Class Actions: An Empirical Comparison*, U. MICH. LAW & ECON. RESEARCH PAPER NO. 12-022; N.Y.U. LAW & ECON. RESEARCH PAPER NO. 12-38 (Feb. 25, 2014), available at http://papers.ssrn.com/ol3/papers.cfm?abstract_id=2109739.

57. *Id.*

58. *Id.*

II. NEW RULES AND REGULATIONS FROM THE SEC

A. OCR Rulemaking on NRSROs

On January 20, 2011, the SEC adopted rules that required NRSROs to disclose certain information to investors on representations and warranties on the rating of asset-backed securities.⁵⁹ The SEC has also proposed rules regarding the remaining requirements of Dodd-Frank on the regulation of NRSROs on May 18, 2011.⁶⁰ These proposed rules are “designed to improve the practices of credit rating agencies, including rules to limit the conflicts that may arise when NRSROs rely on client payments to drive profits and rules to monitor rating agency employees who move to new positions with rated entities.”⁶¹ On December 27, 2013, the SEC adopted final rules required by Dodd-Frank that removed references to credit ratings in certain financial regulations in the Securities Exchange Act of 1934⁶² and under the Investment Company Act of 1940 and the Securities Act of 1933.⁶³ Although intended to protect investors from reliance on credit ratings of securities, these final rules do not address the conflict of interest issues addressed in the proposed rules issued May 18, 2011.⁶⁴ Also in December 2013, SEC staff issued an annual report on its findings of examinations of 10 NRSROs.⁶⁵

59. Disclosure for Asset-Backed Securities Required by Section 943 of the Dodd-Frank Wall Street Reform and Consumer Protection Act, 17 C.F.R. §§ 229, 232, 240, 249 (2011).

60. 17 C.F.R. §§ 232, 240, 249, 249(b) (2011), available at <http://www.sec.gov/rules/proposed/2011/34-64514.pdf>.

61. *Implementing the Dodd-Frank Wall Street Reform and Consumer Protection Act*, U.S. SEC. & EXCH. COMM’N, <http://www.sec.gov/spotlight/dodd-frank.shtml> (last modified Apr. 18, 2014).

62. Available at <http://www.sec.gov/rules/final/2013/34-71194.pdf>.

63. Available at <http://www.sec.gov/rules/final/2013/33-9506.pdf>.

64. See *supra* note 60 (Dodd-Frank requires rules on the regulation of NRSROs in the following areas: filing annual reports on internal controls; addressing conflicts of interest with respect to sales and marketing concerns; conducting “look-back” reviews of ratings in which former NRSRO employees participated to determine whether employment opportunities with a rated entity, issuer, underwriter, or sponsor influenced the rating; disclosing information relating to initial credit ratings and subsequent changes to credit ratings to track the performance of an NRSRO’s credit ratings; requiring an NRSRO to have certain policies and procedures governing the way an NRSRO determines credit ratings; publishing a standard form with each credit rating disclosing, among other things, the assumptions underlying the methodology used to determine the credit rating; disclosing information concerning third party due diligence reports for asset-backed securities; establishing professional standards for training credit rating analysts; and requiring the consistent application of rating symbols and definitions).

65. *2013 Summary Report of Commission Staff’s Examinations of Each Nationally Recognized Statistical Rating Organization*, available at http://www.sec.gov/news/studies/2013/nrsro-summary-report-2013.pdf?utm_source=page&utm_medium=/financial-reporting-network/insights/2014/sec-addresses-credit-ratings-nrsros.aspx&utm_campaign=download; (The

To receive public comments on various matters relating to credit ratings, the SEC created a Credit Ratings Roundtable.⁶⁶ The Roundtable has had three panels: one to examine issues on creating a credit rating assignment system, another to address the effectiveness of the SEC's current system for encouraging unsolicited ratings of asset-backed securities, and another to focus on potential alternatives to the current issuer pay business model.⁶⁷ The Roundtable discussion took place on May 14, 2013, and comments on issues addressed were accepted until June 3, 2013.⁶⁸ As of May 2014, the Roundtable has not held additional meetings, public panels, or solicited comments.⁶⁹

Dodd-Frank's mandate on the OCR to solve perceived problems created by the "big three" credit rating agencies (Fitch, Moody's and S&P) has not been accomplished, as the SEC's proposed rules on regulation of NRSROs to prevent conflict of interest and undue influence on the financial markets have yet to be finalized.⁷⁰ In addition, credit rating industry thought leaders believe the OCR's proposed rules do not help NRSROs create transparency of credit rating methodologies, do not reduce the costs associated with becoming an NRSRO, and do not address the inherent conflict of interest existing in the current "issuer pay" model of the credit rating system.⁷¹

B. Corporate Governance and Compensation Disclosure Provisions

While Dodd-Frank primarily focuses on regulating financial services and markets, the scope of its corporate governance and compensation disclosure

report reviewed 10 NRSROs, A.M. Best Company, Inc. ("AMB"), DBRS, Inc. ("DBRS"), Egan-Jones Ratings Company ("EJR"), Fitch Ratings, Inc. ("Fitch"), HR Ratings de México, S.A. de C.V. ("HR"), Japan Credit Rating Agency, Ltd. ("JCR"), Kroll Bond Rating Agency, Inc. ("KBRA"), Moody's Investors Service, Inc. ("Moody's"), Morningstar Credit Ratings, LLC ("Morningstar"), Standard & Poor's Ratings Services ("S&P") and states the finding and recommendations of staff in the areas Adherence to Policies, Procedures, and Methodologies; Management of Conflicts of Interest; Implementation of Ethics Policies; Internal Supervisory Controls, Governance, Designated Compliance Officer Activities, Complaints, and Post-Employment).

66. *Credit Ratings Roundtable*, U.S. SEC. & EXCH. COMM'N (Apr. 23, 2013), <http://www.sec.gov/rules/other/2013/34-69433.pdf>.

67. *Id.*

68. *Id.*

69. *Other Commission Orders, Notices, and Information*, U.S. SEC. & EXCH. COMM'N, <http://www.sec.gov/rules/other.shtml> (last modified May 2, 2014).

70. See Jeffrey Manns, *Downgrading Rating Agency Reform*, 81 GEO. WASH. L. REV. 749 (2013) (describing the SEC's rulemaking challenges of resolving the conflict of interests problems in the present credit rating system and the failure to craft benchmarks for rating agency performance that hold them accountable).

71. See Robinson, *supra* note 38 (discussing the continued complications even after the formation of the Office of Credit Ratings).

provisions are much broader, affecting all publicly-traded firms.⁷² In implementing Dodd-Frank, the SEC has adopted, proposed, or considered rules related to proxy access, “Say-on-Pay,” relationship of pay and performance, management hedging policies, and compensation committee independence, including additional disclosures related to the compensation committee’s use of compensation advisers and existing conflicts of interest.⁷³ Dodd-Frank continues the trend of regulatory bodies mandating additional disclosure in an attempt to “fix” perceived problems by ensuring transparency and providing additional information to users in order to assist the recipients in making better-informed decisions.⁷⁴ While some of the regulations have now been in place for a couple of years (e.g., Say-on-Pay),⁷⁵ others are still being proposed. In September 2013, the SEC proposed its most recent executive compensation disclosure rule mandated by Dodd-Frank which requires companies to disclose the ratio of total CEO compensation to the median of the annual total compensation of all employees of the firm except the CEO (the “Pay Ratio”).⁷⁶

We proceed by briefly describing the status of the Say-on-Pay and Pay Ratio executive compensation disclosures mandated by Dodd-Frank and proposed or adopted by the SEC. The experience of the SEC in proposing these regulations in the executive compensation area appear to be a microcosm of the overall experience of attempts to implement Dodd-Frank across the board, given the complexity of the legal and economic issues involved.

I. Say-on-Pay.—Under Section 951 of Dodd-Frank, public companies are required to offer shareholders the opportunity to have an advisory vote on executive compensation, along with an additional advisory vote on the frequency of the Say-on-Pay vote.⁷⁷ To implement the Dodd-Frank mandate, the SEC adopted final Say-on-Pay regulations in January 2011, requiring companies to include a resolution in its proxy statement asking shareholders to approve in a non-binding advisory vote the compensation of their executive officers disclosed in the proxy.⁷⁸ This concept was not a new one, as similar regulations had been in place in the United Kingdom since 2003 and many U.S. firms had been subject to shareholder proposals related to Say-on-Pay under the existing rules for shareholder proposals.⁷⁹ In addition, the SEC regulations also require a separate

72. 12 U.S.C. § 5221 (2009).

73. *See generally* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

74. *Id.*

75. *SEC Adopts Rules for Say-on-Pay and Golden Parachute Compensation as Required Under Dodd-Frank Act*, U.S. SEC. & EXCH. COMM’N (Jan. 25, 2011), <http://www.sec.gov/news/press/2011/2011-25.htm>.

76. Pay Ratio Disclosure, 17 C.F.R. §§ 229, 249 (2013).

77. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 951, 124 Stat. 1376, 1899 (2010).

78. Shareholder Approval of Executive Compensation and Golden Parachute Compensation, 17 C.F.R. §§ 229, 240, 249 (2011).

79. *See generally* Randall S. Thomas et al., *Dodd-Frank’s Say-on-Pay: Will It Lead to a*

resolution as to frequency of the Say-on-Pay resolution, which can range from between one and three years.⁸⁰

According to the *Wall Street Journal*, most firms have elected to have annual Say-on-Pay votes, reporting over 80% of firms having annual votes.⁸¹ Also, more than one-half of the companies that originally indicated that they would recommend holding votes every three years eventually elected to have annual votes.⁸²

How have shareholders reacted to the Say-on-Pay disclosure, and in general do shareholders believe that CEOs are overpaid? According to Semler Brossy, an independent executive compensation consulting firm, over 90% of the companies reviewed from the Russell 3000⁸³ have had votes of more than 70% approving the CEO pay package, and 70% of the firms have had approval votes of greater than 90%.⁸⁴ In addition, just above 2% of the firms have failed to receive a majority of votes approving the pay package and these vote proportions have been consistent in each of the three years since Say-on-Pay went into effect.⁸⁵

Thus, shareholders have overwhelmingly approved the Say-on-Pay resolutions, and yet it also appears that the regulation has had little impact on overall compensation levels, as average total compensation levels have continued to rise since 2010.⁸⁶ This is consistent with prior research on the Say-on-Pay regulation adopted in the United Kingdom in 2003 as to compensation levels, but Professors Fabrizio Ferri and David Maber find that pay-for-performance sensitivity has increased.⁸⁷

While the regulations appear to have little effect on the majority of firms, the process has appeared at the very least to have opened up a dialogue about executive compensation between some firms and its investors. For example, Simon Property Group, a leading American commercial real estate company

Greater Role for Shareholders in Corporate Governance?, 97 CORNELL L. REV. 1213 (2013).

80. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 951, 124 Stat. 1376, 1899 (2010).

81. Emily Chasan, *Most Companies Opt for Annual Say-On-Pay Votes*, WALL ST. J. (Apr. 9, 2013, 12:32 AM), <http://blogs.wsj.com/cfo/2013/04/09/most-companies-opt-for-annual-say-on-pay-votes/> (citing a study by Towers Perrin).

82. *Id.*

83. A stock market index measuring the performance of 3000 U.S. publicly traded companies. *Russell 3000 Index*, RUSSELL INVESTMENTS, http://www.russell.com/indexes/data/fact_sheets/us/russell_3000_index.asp (last visited May 15, 2014).

84. Semler Brossy, *2013 Say on Pay Report*, SEMLER BROSSY (Sept. 21, 2013), <http://www.semlebrossy.com/sayonpay>.

85. *Id.*

86. Jesse Eisinger, *In Shareholder Say on Pay Votes, More Whispers than Shouts*, DEALBOOK, N.Y. TIMES (June 26, 2013, 12:00 PM), <http://dealbook.nytimes.com/2013/06/26/in-shareholder-say-on-pay-votes-more-whispers-than-shouts/>.

87. Fabrizio Ferri & David A. Maber, *Say on Pay Votes and CEO Compensation: Evidence from the UK*, 17 *REVIEW OF FINANCE* 2 527-563 (2013).

headquartered in Indianapolis, Indiana, reduced its pay for its President following a negative vote and follow-up discussions with investors about the structure of the compensation.⁸⁸ Therefore, a primary benefit of the Say-on-Pay regulation may be the “improved relationships between boards and institutional investors, rather than improved economic decision-making.”⁸⁹

In evaluating the overall impact of Say-on-Pay, it appears that the required vote has been effective in enhancing the communication between investors and companies related to executive compensation.⁹⁰ Shareholders overwhelmingly approve all but a handful of proposals, and the overall levels of executive compensation have continued to grow after the initiation of Say-on-Pay in the U.S.⁹¹ Professors Cotter, Palmitter, and Thomas state that while “the voting gesture mandated by law might have been mostly empty, placement of the issue on the company’s ballot may have changed the dynamics of the shareholder–management dialogue. Shareholder votes focused negative attention on poorly performing firms with relatively high pay levels.”⁹²

2. *Pay Ratio*.—Unlike the Say-on-Pay regulation that was adopted in final form and went into effect soon after the passage of Dodd-Frank, the Pay Ratio disclosure has had a bumpier path. In September 2013, the SEC approved for comment new proposed rules for implementing Section 953(b) of Dodd-Frank which require: additional disclosures from the firm related to annual total CEO compensation, the median of the annual total compensation of all employees of the firm except the CEO, and the ratio of these two measures.⁹³ The SEC originally expected to finalize these regulations in 2011; however, the provision has been the subject of widespread discussion and debate, with the SEC receiving over 22,000 public comment letters prior to September 15, 2013.⁹⁴ In trying to satisfy the mandate of Dodd-Frank, requiring the specific disclosure while simultaneously fulfilling its mission of investor protection, the SEC states that “The proposed rules to implement Section 953(b) are designed to comply with the statutory mandate and to address commenters’ concerns regarding the potential

88. Kris Hudson & A.D. Pruitt, *Simon Property Changes CEO Pay Package After Criticism*, WALL ST. J. (Apr. 4, 2013, 7:00 PM), <http://online.wsj.com/news/articles/SB10001424127887323916304578403040759610924>.

89. David F. Larcker et al., *Ten Myths of “Say on Pay,”* ROCK CENT. FOR CORPORATE GOVERNANCE AT STAN. U. CLOSER LOOK SERIES: TOPICS, ISSUES, AND CONTROVERSIES IN CORPORATE GOVERNANCE NO. CGRP-26, 4 (June 28, 2012), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2094704.

90. *See* Thomas et al., *supra* note 79, at 1258-59 (discussing how “the new law has led many companies to increase their communication with shareholders and re-evaluate their compensation and corporate governance practices”).

91. *Id.* at 1215.

92. *Id.* at 1265.

93. Pay Ratio Disclosure, Dodd-Frank Act Release (Sept. 18, 2013), *available at* <http://www.sec.gov/rules/proposed/2013/33-9452.pdf>.

94. *Id.* at 6.

costs of complying with the disclosure requirement.”⁹⁵ However, neither the statute nor the related legislative history “directly states the objectives or intended benefits of the provision.”⁹⁶

From one point of view, the pay ratio disclosure may appear to simply add to the transparency of executive compensation, given that firms already are required to disclose the total compensation of the CEO.⁹⁷ Proponents of the disclosure suggest that the information is important to investors seeking information related to executive pay relative to other employees, and the impact of pay structure on productivity and performance, which may in turn allow for more informed voting for directors and for say-on-pay resolutions.⁹⁸ In addition, the internal benchmarking of comparing CEO compensation to the median worker may offset some of the upward bias observed in CEO compensation levels from the practice of benchmarking against peer groups.⁹⁹

However, the calculation of total compensation for the median employee increases the complexity and cost in complying with the regulation for the typical publicly-traded firm.¹⁰⁰ Most firms do not maintain information about each component of compensation for all employees, and it would be extremely costly to do so.¹⁰¹ In the proposing release, the SEC acknowledges that the disclosure “requires registrants to disclose specific information about non-executive employee compensation that is not currently required for disclosure, accounting or tax purposes.”¹⁰² As a result, the SEC tries to accommodate these concerns by allowing some flexibility in determining both the median employee and total compensation.¹⁰³ Although all employees on the last day of the company’s fiscal year must be considered, including part-time, seasonal, and non-US employees, the company is allowed some discretion in its approach to identifying the median

95. *Id.* at 11.

96. *Id.*

97. Press Release, U.S. Sec. & Exch. Comm’n, SEC Proposes Rules for Pay Ratio Disclosure (Sept. 18, 2013), available at <http://www.sec.gov/News/PressRelease/Detail/PressRelease/1370539817895#.Un7mqflJMdU>.

98. See *Overpaid? Or Worth Every Penny*, N.Y. TIMES, July 13, 2013, <http://www.nytimes.com/2013/07/14/opinion/sunday/overpaid-or-worth-every-penny.html> (discussing the potential uses of pay gap information).

99. See Luis A. Aguilar, *Providing Context for Executive Compensation Decisions*, U.S. SEC. & EXCH. COMM’N (Sept. 18, 2013), available at <http://www.sec.gov/News/Speech/Detail/Speech/1370539813937#.UnbeDvlJMdU> (discussing the flawed practice of benchmarking against peer groups for determining executive compensation).

100. *The Dodd-Frank Wall Street Reform and Consumer Protection Act: Impact On Executive Compensation 4* (Dec. 2010), available at <http://www.pwc.com/us/en/financial-services/regulatory-services/publications/assets/closer-look-executive-compensation.pdf>; see also Ike Brannon, *The Egregious Costs of the SEC’s Pay Ratio Disclosure* (May 2014), available at <https://www.uschamber.com/sites/default/files/documents/files/Egregious-Cost-of-Pay-Ratio-5.14.pdf>.

101. *Id.*

102. Pay Ratio Disclosure, *supra* note 93, at 10.

103. *Id.* at 12.

employee.¹⁰⁴ Also, the firm does not need to calculate the value of each of the components that comprise annual total compensation for every employee, but may identify the “median” employee using any compensation measure and then compute the annual total compensation for that employee.¹⁰⁵

While the flexibility allowed by the proposed rule is an attempt by the SEC to make it less costly to implement for firms, the SEC acknowledges that the resulting outcome limits the comparability of the ratio across firms.¹⁰⁶ Thus, the usefulness of the ratio for investors is questionable because the discretion provided to firms prevents investors from making true relative comparisons.¹⁰⁷ The opponents generally have argued that the pay ratio disclosure would be costly, complicated, and potentially inaccurate while providing a disclosure that is immaterial to most investors.¹⁰⁸ In voting against adopting the provision, one of the five Commissioners of the SEC, Michael Piowar, argued that the SEC should not be spending its efforts and resources on “any rulemaking that unambiguously harms investors, negatively affects competition, promotes inefficiencies, and restricts capital formation.”¹⁰⁹ As to the potential benefits of the Pay Ratio, Commissioner Piowar cited the release which “specifically warns that ‘using the pay ratio to compare companies may not be relevant and could generate misleading interpretations or conclusions.’”¹¹⁰ Another dissenting Commissioner, Daniel Gallagher, went further by stating that “There are no—count them, zero—benefits that our staff have been able to discern.”¹¹¹ Continuing, he cited the proposal which states that “[T]he lack of a specific market failure identified as motivating the enactment of this provision poses significant challenges in quantifying potential economic benefits, if any, from the pay ratio disclosure.”¹¹²

Potential legal challenges to the Pay Ratio and other new regulations

104. *Id.* at 12-13.

105. *Id.* at 13.

106. The SEC argues the “precise comparability across companies may not be relevant and could generate potentially misleading interpretations or conclusions.” *Id.* at 93. Also, “the potential value of this disclosure for assessing issues related to employee morale, productivity and investment in human capital may be diminished by the indirect costs of creating incentives for registrants to change their business structure.” *Id.*

107. *Id.* at 71.

108. John Cavanagh, *Comment Letter on Pay Ratio Disclosure*, INST. FOR POL’Y STUD. (Oct. 30, 2013), available at <http://www.sec.gov/comments/s7-07-13/s70713-278.pdf>.

109. Michael S. Piowar, *Statement at Open Meeting Regarding Municipal Advisors and Pay Ratio Disclosure*, U.S. SEC. & EXCH. COMM’N (Sept. 18, 2013), available at <http://www.sec.gov/News/Speech/Detail/Speech/1370539811778#.UnbiqfJMdU>.

110. *Id.*

111. Daniel M. Gallagher, *Dissenting Statement of Commissioner Daniel M. Gallagher Concerning the Proposal of Rules to Implement the Section 953(b) Pay Ratio Disclosure Provision of the Dodd-Frank Act*, U.S. SEC. & EXCH. COMM’N (Sept. 18, 2013), available at <http://www.sec.gov/News/Speech/Detail/Speech/1370539815919#.UnbjOfJMdU>.

112. *Id.* (quoting at Pay Ratio Disclosure, *supra* note 93, at 91).

mandated by Dodd-Frank and promulgated by the SEC are done with the backdrop of the SEC's experience with the so-called "proxy access" rule.¹¹³ Although the SEC had announced its intent to propose a proxy access rule, allowing certain shareholders to include director nominees in the firm's proxy materials even before the passage of Dodd-Frank, Section 971 of Dodd-Frank gave the SEC the authority to adopt such a provision.¹¹⁴ In 2009, the SEC proposed a revised Rule 14a-11, which permitted a shareholder or group of shareholders that had held 1% to 5% of the firm's shares for at least a year to nominate director candidates for up to 25% of the board.¹¹⁵ Almost immediately, the rule was challenged in court, eventually leading to the D.C. Circuit Court striking down the regulation before it was ever officially in effect due in part to an insufficient cost benefit analysis.¹¹⁶ Thus, the dissenting commissioner's concerns about potential costs and benefits of the Pay Ratio disclosure set the stage for another extended debate and potential challenges to the rule.¹¹⁷

CONCLUSION

Following the financial crisis of 2007-2009, Congress passed Dodd-Frank and greatly expanded the regulatory structure around the financial services sector. The SEC's role significantly increased, with requirements for additional agencies to be formed within the SEC along with provisions that mandate additional SEC rulemaking in many cases and that provide for discretionary rulemaking authority in others. In this Article, we discuss the SEC's progress and identify some of the problems associated with attempts to regulate perceived or real conflicts of interest by mandated rules or disclosure.

The challenges in drafting a rule that prevents the inherent conflict of interest associated with the current economic model of credit rating agencies is evident as Dodd-Frank's attempt to solve the problems with NRSRO's influence on the financial markets remains a work in progress. The SEC's proposed rules on regulation of NRSROs to prevent conflict of interest and undue influence have not been finalized and no further meetings of the Roundtable to receive public comments on improving the current credit rating systems has been scheduled since May 2013.

Alternatively, conflicts of interest may be managed if appropriate information is provided to interested parties. To promote transparency in the financial markets, the SEC has a long history of emphasizing disclosure with the goal of

113. See *Facilitating Shareholder Director Nominations*, U.S. SEC. & EXCH. COMM'N (Aug. 25, 2010), available at <http://www.sec.gov/rules/final/2010/33-9136.pdf> (discussing the SEC's proposed proxy access rule).

114. Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 971, 124 Stat. 1376, 1915 (2010).

115. See Jill E. Fisch, *The Destructive Ambiguity of Federal Proxy Access*, 61 EMORY L.J. 435, 445 (2012) (describing the SEC's proxy access rule).

116. *Bus. Roundtable v. Sec. & Exch. Comm'n*, 647 F.3d 1144 (D.C. Cir. 2011).

117. Gallagher, *supra* note 111.

providing useful information to market participants.¹¹⁸ While it appears straightforward that better and more information should lead to improved decision-making, disclosure as a mechanism for ensuring better decision-making has been questioned by a number of commentators. SEC Chair Mary Jo White recently commented in a speech that “[w]hen disclosure gets to be too much or strays from its core purposes, it can lead to ‘information overload’ a phenomenon in which ever-increasing amounts of disclosure make it difficult for investors to focus on the information that is material and most relevant to their decision-making as investors in our financial markets.”¹¹⁹ Specific to disclosure of executive compensation required by the SEC, Professors Steven Davidoff and Claire Hill argue that the enhanced disclosure related to executive compensation has had the unintended consequence of encouraging higher compensation levels for management.¹²⁰ Despite the theory that greater executive compensation disclosure would lead to action, due to real or anticipated shareholder outrage, “[t]he incremental information apparently has not prompted shareholder action, but appears to have prompted action by peer CEOs—to put pressure on their boards to raise their pay.”¹²¹ While the goals of Dodd-Frank are to address and prevent a similar financial crisis from occurring in the future, the use of the SEC’s disclosure framework related to executive compensation appears to be inconsistent. Past attempts to use disclosure as a mechanism for reducing “excessive” executive compensation have not resulted in lower overall levels of executive compensation, which bolsters the arguments of commentators that suggest CEO pay is based on performance and may reflect market-based transactions.¹²²

Given the SEC experience with the proxy access rule, the impact of Say-on-Pay and the discussion both in support of and dissenting from the Pay Ratio proposal is relevant. While questions may exist as to the magnitude of the benefits of the Say-on-Pay rule, it does appear that the introduction of the proposals has affected the dialogue between investors and firms and how firms motivate the levels of executive compensation.¹²³ However, given the advisory nature of the vote, it does not appear to be particularly costly to firms, other than from a reputational standpoint for a few outlier firms, as over 97% of firms have

118. See Mary Jo White, *The Importance of Independence*, U.S. SEC. & EXCH. COMM’N (Oct. 3, 2013), available at http://www.sec.gov/News/Speech/Detail/Speech/1370539864016#.UoOPk_IJMdU (discussing the history of disclosure practices at the SEC).

119. *Id.*

120. Steven M. Davidoff & Claire A. Hill, *Limits of Disclosure*, 36 SEATTLE U. L. REV. 599, 626 (2013).

121. *Id.* at 604.

122. *Id.*; see also Steven Kaplan, *CEO Pay and Corporate Governance in the U.S.: Perceptions, Facts, and Challenges*, 25 J. APPLIED CORP. FIN. 8, 25 (2013) (discussing how shareholder votes are more consistent with a market-based view of top executive pay as opposed to pay driven by managerial power).

123. See Thomas et al., *supra* note 79 (discussing how “say on pay” has created a broader dialogue on pay issues between management and shareholders).

received a positive confirmation from shareholders.¹²⁴

Turning to the Pay Ratio, the split vote among SEC Commissioners in adopting the proposal demonstrates the varied and strong opinions on the potential costs and benefits.¹²⁵ SEC Chair White addressed the difficult position of the SEC given the Congressional mandates of Dodd-Frank in stating that “other mandates, which invoke the Commission’s mandatory disclosure powers, seem more directed at exerting societal pressure on companies to change behavior, rather than to disclose financial information that primarily informs investment decisions . . . as the Chair of the SEC, I must question, as a policy matter, using the federal securities laws and the SEC’s powers of mandatory disclosure to accomplish these goals.”¹²⁶ Given the legislative mandate, however, the SEC must adopt the disclosure rule and attempt to limit or mitigate the costs.¹²⁷ As we move forward and the SEC promulgates additional regulations related to corporate governance and credit ratings, the debate will continue as to the costs and benefits associated with mitigating conflicts of interest and providing helpful disclosure to investors and other market participants.

124. See *Homogenization of Executive Pay Plans: The Unintended Consequences of Say on Pay Votes*, Pay Governance, available at <http://paygovernance.com/homogenization-of-executive-pay-plans-the-unintended-consequences-of-say-on-pay-votes-2/> (last visited May 15, 2014).

125. Jessica Holzer, *SEC, in Split Vote, Adopts ‘Say on Pay’ Rule*, WALL ST. J. (Jan. 25, 2011, 6:25 PM), available at <http://online.wsj.com/news/articles/SB10001424052748704698004576104071862597358>.

126. White, *supra* note 118.

127. *Id.*