Testimony of Alexander F. Cohen
Partner
Latham & Watkins LLP[1]

Before the U.S. House of Representatives
Committee on Financial Services
Subcommittee on Capital Formation

"A New Day at the SEC: Restoring Accountability, Due Process, and Public Confidence"

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Chair Wagner, Ranking Member Sherman, and Members of the Subcommittee,

Thank you for inviting me to appear before you today.

I've been practicing as a securities lawyer for nearly 36 of my 38-year legal career. During this time I had the honor to serve as the Deputy General Counsel for Legal Policy and Administrative Practice at the U.S. Securities and Exchange Commission (SEC), and later as the SEC's Deputy Chief of Staff to then-SEC Chairman Christopher Cox.

This experience has led me to two over-arching conclusions about the U.S. securities laws.

First, the U.S. securities laws have been remarkably successful in making the United States the gold standard of securities regulation.

Second, in the nearly 93 years since the passage of the Securities Act of 1933, the securities regulatory system has accumulated numerous features that, like barnacles on the hull of a ship, serve only to slow down progress.

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[1] The views and opinions I express below are solely my own and do not necessarily reflect the views of Latham & Watkins LLP or the firm's clients.

Congress now has the opportunity to sandblast these regulatory impediments off. And I'm grateful to the Subcommittee for the opportunity to contribute some sand to this undertaking.

In the Appendix to my testimony, I describe a package of 10 improvements that Congress can make to the existing SEC functioning and U.S. securities regulation, organized into four broad categories:

- modernizing the SEC's structure;
- improving the SEC's regulation of public company accountants;
- reining in SEC regulatory overreach; and
- eliminating regulatory inefficiencies and failed initiatives.

I recognize that my proposals range from the far-reaching to the quite technical. But I am convinced that all would help assure that the United States retains its position as the leader of global securities regulation.

I welcome your questions.

Appendix

10 Improvements Congress Can Make to the SEC and U.S. Securities Regulation

I. MODERNIZING THE SEC'S STRUCTURE

1. *Amend the Exchange Act to create the position of Vice Chairman*

- The SEC has become sufficiently large and its work sufficiently complex that it needs to have a Vice Chairman in addition to the Chairman. The Chairman has too many responsibilities and too many direct reports to function with maximum effectiveness. These include important statutory responsibilities outside the agency, such as being one of the voting members of the Financial Stability Oversight Council and a member of the Federal Housing Finance Oversight Board.

- The need to meet these constant operational pressures make it difficult for any Chairman to find time engage in setting strategic direction in the face of the press of day-to-day business.

- The Chairman cannot effectively delegate these responsibilities to Commissioners or Staff members, who do not exercise the Chairman's authority.

- Congress should accordingly amend the Exchange Act to create the position of Vice Chairman.

II. IMPROVING REGULATION OF PUBLIC COMPANY ACCOUNTANTS

2. *Amend the Sarbanes-Oxley Act to make the PCAOB an office within the SEC*

- The Public Company Accounting Oversight Board (PCAOB) was created by Congress in the 2002 Sarbanes-Oxley Act to regulate the public accounting profession. However, it was set up as a private entity.

- After nearly 24 years, the time has come to recognize that the PCAOB's anomalous status as a private entity exercising important governmental functions has come at a significant cost.

- In particular, it has led to excessive spending with limited accountability. As Commissioner Peirce noted in her Statement at the Open Meeting to Consider the Public Company Accounting Oversight Board's 2025 Final Budget and Accounting Support Fee:

> The PCAOB is asking for nearly $400 million for 2025. While only a 4% increase from 2024, it is 40% higher than 2020's $285 million request. At this rate, the budget five years from now will be $560 million. The increase is striking, but even more important is

> whether the PCAOB is having a net positive effect on audit quality. Are the dollars the PCAOB is spending working? The PCAOB paints a picture that does not look a lot better than pre-PCAOB days. (footnotes omitted)

- The SEC's recent approval of a reduced 2026 budget for the PCAOB – which notably includes a 52% and 42% reduction in the Chairperson and other Board members' compensation – is a welcome step in the right direction.[2] But Congress should go further. It should eliminate the status of the PCAOB as a private entity, and should instead make the PCAOB an office within the SEC, subject to full Congressional oversight.[3]

III. REINING IN SEC OVERREACH

3. *Amend Securities Act Section 2(a)(11) to clarify that a person who provides services to facilitate a securities offering but does not participate in distribution-related activities is not a statutory underwriter*

    - Under Chair Gensler, the SEC attempted to use Section 2(a)(11) to impose underwriter status on persons not intended to be covered by the statutory definition, such as those whose involvement in a securities offering consists of acting as a financial advisor. In particular, the SEC proposed Securities Act Rule 140a to broaden significantly the type of activities that would give rise to underwriter liability. *See* the SEC's SPAC Proposal, Release No. 33-11048 at 96-101. Proposed Rule 140a met with significant criticism from commenters. *See, e.g.,* Comment Letter from the Securities Industry and Financial Markets Association on the SEC's SPAC Proposal (discussing the defects of proposed Rule 140a in detail).

    - Even though abandoned by the SEC, the uncertainties created by proposed Rule 140a have caused market participants to take various defensive steps, thereby increasing the cost and complexity of capital-raising exercises such as de-SPAC transactions.

    - Congress should amend Section 2(a)(11) of the Securities Act to make clear that persons with only incidental connections to a securities offering will not be deemed a statutory underwriter.

4. *Amend Exchange Act Section 14(a) to clarify that it applies to proxy voting advice provided by advisory firms for a fee and direct the SEC to rescind the rollback of the 2020 proxy advisory firms rules*

    - After decades of public debate, the SEC in 2020 amended its proxy rules (the 2020 rules) to impose enhanced disclosure and procedural requirements on firms, such as

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[2] *See* https://www.sec.gov/newsroom/press-releases/2026-11-sec-approves-2026-pcaob-budget-accounting-support-fee.

[3] This change could be accomplished with a limited number of amendments to Title I of the Sarbanes-Oxley Act of 2002.

Institutional Shareholder Services and Glass Lewis, that provide proxy voting advice to institutional shareholders and investment advisers.

- Under Chair Gensler's leadership, the SEC announced that it would not enforce certain provisions of the 2020 rules one month before they were scheduled to go into effect, and in 2022, the SEC adopted amendments to the proxy rules to roll back some of the provisions of the 2020 rules.

- Extensive litigation in response to the SEC's actions has resulted in a federal circuit split. Notably, in a decision rendered in February 2024, the U.S. District Court for the District of Columbia disputed the SEC's authority to regulate proxy advisory firms under Section 14(a).

- Meanwhile, proxy advisory firms continue to play an outsized role in the proxy voting process, including exerting significant influence over matters that public companies put to shareholder vote, with very little transparency and regulatory oversight. The President's recent Executive Order on proxy advisors lays out some of these issues.

- To provide the SEC with the unquestionable authority to regulate proxy advisory firms under the proxy rules, Congress should amend Exchange Act Section 14(a) to clarify that the term "solicit" covers the provision of proxy voting advice for a fee. Also, it should direct the SEC to reinstate the 2020 rules in their entirety.

5. *Direct the SEC to amend Exchange Act Rule 10D-1 to conform the rule to the statutory mandate in Exchange Act Section 10D, which only covers "Big R" restatements and executive officers as a predicate for compensation clawbacks, by eliminating Rule 10D-1's coverage of "little r" restatements and non-executive officers*

- Section 954 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (adding Section 10D to the Exchange Act) mandated SEC rulemaking for listed companies to claw back incentive compensation if "the issuer is required to prepare an accounting restatement due to the ***material noncompliance*** of the issuer with any financial ***reporting*** requirement under the securities laws" (Exchange Act Section 10D(b)(2); emphasis added).

- 13 years later, the SEC finally adopted rules under Exchange Act 10D. However, Rule 10D-1 as adopted under Chair Gensler in 2023 expanded the predicate for clawbacks beyond the statutory authorization in Exchange Act Section 10D in two ways:
    - First, Rule 10D-1 requires compensation clawbacks after a "little r" restatement, which is a type of immaterial error correction that involves ***no publicly reported material error*** and therefore ***no material noncompliance*** with any financial reporting requirement. According to the Rule 10D-1 Adopting Release, Release

No. 33-11126, this extension generated an over-fourfold increase in the rule's scope over and above that of the statute.[4]

- o Second, Rule 10D-1 requires compensation recovery for a broader group of persons than "executive officers" as defined under Exchange Act Rule 3b-7, whereas Section 10D contemplates a mandatory clawback policy that applies only to "any current or former executive officer of the issuer." Rule 10D-1 defines "executive officer" in conflict with the Exchange Act definition and instead confusingly tracks the Section 16 definition of "officer" in Rule 16a-1(f), which includes the principal accounting officer (or controller, if there is no such accounting officer) even if that person is not a Rule 3b-7 executive officer.

- Congress should accordingly direct the SEC to amend Rule 10b-1 to conform the rule to the statutory mandate in Exchange Act Section 10D, which covers only "Big R" restatements and executive officers as a predicate for compensation clawbacks, by eliminating Rule 10D-1's coverage of "little r" restatements and person who are not executive officers.

IV. ELIMINATING REGULATORY INEFFICIENCIES AND FAILED INITIATIVES

A. Regulatory Inefficiencies

6. *Amend Exchange Act Section 15(d) to eliminate the requirement to provide a terminal annual report on Form 10-K/20-F*

- Exchange Act Section 15(d) provides that an issuer may suspend Exchange Act reporting in any year with respect to any class of securities, if it had fewer than 300 holders of record at the beginning of that year, other than a year in which it has had a registration statement that became effective under the Securities Act.

- The SEC accordingly requires issuers that have suspended reporting under Section 15(d) to provide an annual report on Form 10-K or 20-F in respect of the fiscal year after which an issuer has deregistered and ceased reporting (a terminal 10-K/20-F).

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[4] *See Release* No. 33-11126 at 8 n.14, & 129 n.396, citing Memorandum, SEC Division of Economic and Risk Analysis (June 8, 2022) at 3-4 (indicating that, in 2021, "Big R" restatements represented less than one-fourth of the 227 total "Big R" and "little r" restatements combined and acknowledging, with some understatement, that a 420% expansion of Rule 10D-1's scope "would increase the total number of restatements that could potentially trigger a compensation recovery analysis"); *see also* DERA Memorandum at 3 & n.18 (indicating that, in 2020, the number of "Big R" restatements represented less than one-fourth of total "Big R" and "little r" restatements combined), available at https://www.sec.gov/comments/s7-12-15/s71215-20130560-298718.pdf.

- This forces issuers to spend time and resources on Exchange Act reporting at a time when the company has ceased reporting (gone dark). Shareholders of a company that has gone dark derive little additional benefit from a terminal 10-K/20-F, which is in any event focused on the past and not on ongoing issues.

- Congress should amend Section 15(d) to eliminate the requirement to provide a terminal 10-K/20-F.

7. *Amend Exchange Act Section 11(d) to exempt transactions in which securities are sold to QIBS under Securities Act Rule 144A*

- Exchange Act Section 11(d)(1) prohibits any person who is both a broker and a dealer from extending or maintaining credit, or arranging for the extension or maintenance of credit, to or for a customer on any security (other than an exempted security) which was part of a distribution of a new issue of securities in which the broker-dealer participated.

- Even making the questionable assumption that transactions in which securities are sold to qualified institutional buyers (QIBs) in private offerings under Securities Act Rule 144A amount to a "distribution," QIBs are super-heavyweight institutions and do not need the protection provided by Section 11(d)(1). This provision was enacted to prevent abuses associated with broker-dealers enticing unsophisticated investors to purchase securities by offering to finance investment in securities being sold by the broker-dealers.

- Congress should amend Section 11(d) to exempt transactions in which securities are sold to QIBs under Rule 144A.

B. Failed Initiatives

8. *Repeal Exchange Act Section 13(p), added by Section 1502 of the Dodd-Frank Act, which directs the SEC to require public companies to report on their use of conflict minerals*

- Congress added Section 13(p) in an attempt to address human suffering in central Africa by having public companies report on their supply chains.

- The GAO has found that the SEC's rule has not reduced violence and may actually be associated with a spread of violence. Whatever U.S. Government policy response is appropriate to address events in central Africa, it surely does not involve placing ineffective disclosure burdens on public companies.

- Congress should adopt legislation to repeal Section 13(p). It should also immediately rescind the SEC's rules under Section 13(p), so that public companies can immediately get the benefit of the repeal of Section 13(p) without having to wait for SEC rulemaking.

9. *Repeal Exchange Act Section 13(q), added by Section 1504 of the Dodd-Frank Act, which directs the SEC to require public companies engaged in the commercial development of oil, natural gas or minerals to report on their payments to the U.S. federal government or a foreign government*

- Congress added Section 13(q) in 2010 in an attempt to bring greater transparency to payments made to governments in connection with commercial development of oil, natural gas and minerals.

- The SEC's rulemaking under Section 13(q) has had a tortured history. The SEC initially adopted implementing rules in 2012. Those rules were vacated by the U.S. District Court for the District of Columbia in 2013. The SEC then adopted revised rules to implement Section 13(q) in 2016. Those rules were disapproved pursuant to the Congressional Review Act by a joint resolution of Congress in 2017. The SEC adopted further revisions in 2020. The 2020 revisions had a compliance date in 2024, some 14 years after the initial adoption of Section 13(q).

- Section 13(q) results in burdensome disclosure of little value to investors. Nor has it resulted in discernable impact on corruption in resource-rich countries.

- Congress should adopt legislation to repeal Section 13(q). It should also immediately rescind the SEC's rules under Section 13(q), so that public companies can immediately get the benefit of the repeal of Section 13(q) without having to wait for SEC rulemaking.

10. *Repeal Exchange Act Section 13(r), which requires public companies to disclose on a quarterly basis all transactions with certain Iranian-related entities regardless of the amount involved (which is frequently minimal), even if such transactions are lawful, for example are permitted under a license or are not subject to the US sanctions regime*

- This statute, enacted during the Obama administration, does not further national security, since the required disclosure sweeps in transactions that are lawful.

- Public companies nonetheless must implement pervasive and costly controls to capture highly immaterial transactions so that they can be disclosed pursuant to this mandate. Private U.S. companies and foreign companies not listed in the United States are not subject to a similar requirement, placing U.S. public companies at a significant disadvantage with little apparent gain in investor protection.

- Congress should repeal Section 13(r).[5]

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[5] The SEC has not adopted rules to implement Section 13(r), hence no Congressional action is needed in that regard.