Senators queried Jay Clayton at his confirmation hearing to be SEC Chairman on a range of topics, including how he would deal with potential conflicts of interest, his views on enforcement, and why he thinks initial public offerings have dwindled in the U.S. In both his prepared remarks and in his testimony he said the protection of investors is a fundamental responsibility that he would pursue with "energy and purpose," warned there is "zero room for bad actors in our capital markets," and pledged "no favoritism." Clayton spoke most expansively about capital formation and IPOs, two areas he focused on in private practice. President Trump announced Clayton’s nomination in January.

Conflicts and enforcement. Senate Banking Committee Chairman Michael Crapo (R-Idaho) opened the questioning by asking Clayton about how potential conflicts arising from his prior private practice might impact him as SEC chairman. Clayton said he did not believe his prior legal work would impair his SEC duties. The nominee elaborated by saying that recusals would be manageable because the other commissioners could act in specific matters.

Ranking Member Sherrod Brown (D-Ohio) followed with questions about a matter involving allegations that a Trump casino violated rules about non-GAAP financial disclosures. Clayton reiterated his pledge of showing no favoritism. When asked by Brown about Clayton’s contacts with the Trump transition team, Clayton said he had been asked his thoughts on capital markets and the prospect of public service, and that he spoke with several members of the team, including screeners, now-President Trump, Chief of Staff Reince Priebus, and the president’s chief strategist, Stephen Bannon. Clayton agreed to provide Brown with a reconstructed list of those he spoke with about the SEC nomination.

In a second round of questions, Sen. Warren would return to questions about conflicts and enforcement. Specifically, she asked about Carl Icahn, a special adviser to Trump, who is a renowned activist investor with extensive holdings, which Warren suggested he may not have divested since taking on his advisory role in the White House. During the exchange, Clayton said he had met with Icahn after being nominated and that they talked about activist investing, but without discussing specific matters.

Senator Warren later asked if Clayton would avoid talking to Icahn if confirmed. Clayton said he would talk to all types of market participants, while he acknowledged that, in the context of an ongoing investigation of someone, those talks may be inappropriate. In reply to the senator’s question about one of Icahn’s alleged recent investments and insider trading, Clayton said only that insider trading cases are dependent on the facts and circumstances.

On a related point, Sen. Mark Warner (D-Va) had previously mentioned the 10-day Schedule 13D window, which can benefit activist shareholders by allowing accumulation of shares prior to the required public disclosure.
Clayton said shareholder activism is an ongoing debate, but that the purpose of Section 13 reporting should be to incentivize those who see problems with companies, but not to give an unfair advantage.

Acting SEC Chairman Michael Piwowar's widely reported effort to limit who among the SEC’s staff may use the subpoena power brought questions for Clayton by Sen. Robert Menendez (D-NJ). Senator Menendez specifically wanted to know if Clayton was aware of any abuse of the power by SEC staff. Clayton said he had no idea if SEC staff had abused that authority. Clayton also said he was not consulted on the change.

As the hearing ended, Chairman Crapo and Sen. Warren engaged in a brief battle of news sources over whether Republicans or Democrats are weaker on enforcement matters. Senator Warren had earlier claimed that Republicans had a lighter touch on enforcement, but Crapo offered a different set of news reports as evidence that most enforcement decisions by the Commission are unanimous. The SEC’s Office of Freedom of Information Act Services released data on enforcement matters last year. Senator Warren held to her source, which she said indicated that 48 matters during former Chair Mary Jo White’s tenure could not be pursued because of conflicts.

IPO markets. In what may have been Clayton’s signature issue, the SEC nominee dramatically explained why there are so few U.S. IPOs in reply to a question from Sen. Bob Corker (R-Tenn). Using a hand gesture approximating the "hockey stick" pattern of economic growth following a typical recession, but in this context being used to illustrate a company’s growth pattern, Clayton said many companies historically sought to go public at a lower point on the growth chart than is possible today.

Clayton said the costs and other burdens of going public prevent many companies from doing so earlier in their growth cycles. Clayton also said "robust" private capital markets contributed to companies deciding to stay private longer and then going public only after they have reached greater maturity.

In earlier questioning from Chairman Crapo, Clayton had explained that an easier IPO on-ramp, but not eased regulatory standards, already had made a difference in the marketplace. Clayton, a transaction lawyer whose practice emphasizes capital formation, said often times the first question a person will ask about a company is whether it is an emerging growth company under the JOBS Act because EGC status makes an IPO easier.

Individual accountability. Senators also asked Clayton more generally about his views on enforcement, although much of the questioning about enforcement was tinged by suggestions of Clayton, if confirmed, having to pilot the SEC in the context of an Administration that has many potential conflicts of interest.

Senator Heidi Heitkamp (D-ND) asked about clarifying the mental state required to hold company executives criminally responsible. Clayton said that was a question for the courts and Congress, but he would vigorously enforce the law as it is. In reply to a related question from Sen. Catherine Cortez Masto (D-Nev), Clayton said that while companies should be held accountable, individual accountability can be a more effective deterrent.

Dodd-Frank and regulatory approach. The big question for securities practitioners since the November election has been whether the Trump Administration and the Republican-led Congress would follow through on their plans to repeal and replace the Dodd-Frank Act. Senator Brown asked Clayton about the Trump Administration’s related executive order mandating a review of financial system rules. Clayton said he had "no specific plans for attack" on Dodd-Frank, but he also said the reform law should be examined to see if it has achieved its objectives.

On another front, Sen. Richard Shelby (R-Ala), the immediate former Banking Committee chairman, wanted to know how Clayton views the role of cost-benefit analysis in rulemaking. According to Clayton, economic analysis is "very important" both qualitatively and quantitatively. Clayton elaborated by noting that one can look back decades and see the "profound" effects of some regulations.

In reply to a question posed by Sen. Corker, Clayton spoke briefly about partisanship and his approach to voting at the Commission. The senator had asked why the SEC seems so partisan lately. Clayton first said that his goal as chairman would be "consensus" because he values unanimous votes on important matters. But Clayton also "speculate[d]" that partisanship "is strong in Washington," while noting that the SEC’s mission is not a partisan mission.
On a related matter, Sen. Mike Rounds had asked Clayton if he is a Republican. Clayton explained that he is an Independent. Many will recall that former Chairs White and Mary Schapiro described themselves as Independents.

When asked by Sen. Brian Schatz (D-Hawaii) what legal basis Acting Chairman Piwowar had for not pursuing Congressionally-mandated rules, Clayton said that rulemaking required under statute should go forward. Clayton also explained that generally he prefers less complexity and more clarity in regulations, at least to the extent practicable.

Acting Chairman Piwowar also had requested renewed public comment on the Commission’s pay ratio rule. Senator Menendez characterized Piwowar’s action as obstructing implementation of a Congressional mandate and asked Clayton if he agreed with that action. Clayton replied that it was Piwowar’s decision to make and he did not know what prompted the acting chairman to seek more public comment. Clayton said he could not say what he would do if confirmed to be chairman since he has not had an opportunity for interaction with SEC staff on the rule.

With respect to cybersecurity, Sen. Warner wondered if the SEC should take a “fresh look” at cyber issues in light of the Yahoo! Inc. disclosures. Clayton declined to speak about any specific case, but he did suggest that there is a question of whether this type of disclosure is where it should be. During a follow-up exchange with Sen. Jack Reed (D-RI), who has previously introduced legislation to require company boards to disclose their cybersecurity expertise, Clayton further suggested current cyber disclosures may not be enough, but that materiality is the touchstone.