



UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

THE CHAIRMAN

July 30, 2010

The Honorable Christopher J. Dodd
Chairman
Committee on Banking, Housing, and Urban Affairs
United States Senate
534 Dirksen Senate Office Building
Washington, D.C. 20510-6075

Dear Chairman Dodd:

I am writing to address recent assertions that section 929I of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act) was “hidden” in the financial reform legislation and “exempts” the SEC from the Freedom of Information Act (FOIA). As you know, these assertions are false.

The Dodd-Frank Act mandates a number of new responsibilities for the SEC to protect investors, including new authority over hedge funds, private equity funds and venture capital funds. Fulfilling these responsibilities will require the SEC to expand and improve our examination and surveillance capabilities in order to provide the type of risk-focused regulatory oversight investors deserve. In order for our efforts to be successful, it is important that registered entities be able to provide us with access to confidential information without concern that the information will later be made public.

The need for Section 929I is not new, nor is the general language that it contains. As far back as 2006, then SEC Chairman Chris Cox sought language similar to what is contained in Section 929I. On September 11, 2008, the House of Representatives passed H.R. 6513, the Securities Act of 2008, by voice vote with bipartisan support. Section 15 of H.R. 6513 contains language similar to Section 929I. In July 2009, I provided you and other Congressional members with legislative proposals that Commission staff believed would allow the Commission to better protect investors. Contained in those proposals was language similar to Section 929I regarding the protection of certain information provided to the Commission. After receiving these proposals, they were placed on the House Capital Markets Subcommittee website. The Wall Street Reform and Consumer Protection Act that passed the House on December 11, 2009 contained Section 7409, Protecting Confidentiality of Materials Submitted to the Commission, with language that again was very similar to the language in Section 929I. Finally, the Conference Committee’s base text contained Section 929I.

Section 929I addresses a significant and longstanding impediment to the agency’s ability to quickly obtain important information from entities registered with the SEC when performing examinations. In our examination and surveillance efforts, we often seek to gather highly

sensitive and proprietary information and records from regulated firms including, for example, customer information, trading algorithms, internal audit reports, trading strategy information, portfolio manager trading records and exchanges' electronic trading and surveillance specifications and parameters. Such information is critical for us to effectively perform our oversight function and detect possible misconduct. Prior to the Dodd-Frank Act, regulated entities not infrequently refused to provide Commission examiners with sensitive information due to their fears that it ultimately would be disclosed publicly. Existing FOIA exemptions were insufficient to allay concerns due in part to limitations in FOIA (including that certain existing exemptions may not apply to all registrants)¹ and the fact that FOIA exemptions are not applicable when the SEC must respond to a subpoena (as either a party or non-party).² The Commission's resulting inability to obtain this information hindered our capacity to enforce the securities laws and protect investors.

For example, given the amount of automated trading in our markets, it is critical for anti-manipulation purposes that the SEC be able to obtain, review and potentially deconstruct these highly proprietary algorithmic formulas. High-frequency trading firms, however, have been reluctant to provide these formulas to the SEC out of a concern that if they were deconstructed or the data within them were merged into central databases, the SEC might be forced to disclose them under FOIA. Both investors and our markets suffer as a result. Similarly, to assess if insider trading has occurred at certain regulated entities, SEC staff have needed to review personal trading records of investment management personnel. Advisers routinely refuse to turn over such materials for fear of public disclosure, instead requiring staff to review hard copies of the records on the adviser's premises. This limitation materially impacts the staff's ability to detect insider trading activity.

Section 929I of the Dodd-Frank Act addresses these and other related issues head-on. It provides certainty to registrants by clarifying that the information the Commission receives in its examination or surveillance efforts cannot be compelled by third parties, and also enables the SEC to protect the confidentiality of the data and information it receives that is extrapolated and consolidated into surveillance or risk assessment databases. Protecting the confidentiality of this information makes sense, as the non-public or proprietary nature of those documents should not be lost simply because registrants provide the documents to the Commission in connection with its oversight responsibilities.

This provision does not provide a "blanket" SEC exemption from FOIA and is not designed to protect the SEC as an agency from public oversight and accountability. Instead,

¹ For example, FOIA exemption (b)(8) protects matters that are "contained in or related to examination, operating or condition reports prepared by, on behalf of, or for the use of an agency responsible for the regulation or supervision of financial institutions" (emphasis added).

² With respect to subpoenas, the staff is forced to contest them on grounds such as relevance and common law privileges. Depending on how a judge resolves the issues, the SEC may be ordered to produce sensitive records received from a registered entity to the firm's competitors. In some cases, the firms whose records could be disclosed have not even been parties to the proceeding in which the subpoena had been issued. Such disclosures obviously may cause significant harm to the businesses whose records and information are disclosed, and to the integrity of our examination program.

Section 929I is meant to ensure that the Commission can gather the information it needs to perform its required examination, enforcement and oversight duties, including proprietary and customer information. In addition, included within the provision are specific carve-outs that make clear that the Commission may not use the provision to withhold information from Congress, other federal agencies or from a court in response to an order in an action brought by the Commission or the United States. To address any uncertainty about how we will use Section 929I, I am asking the Commission to issue and publish on our website guidance to our staff that ensures the provision is used only as it was intended.

Stated simply, Section 929I is critical to our ability to develop a robust examination program that better protects investors. It will allow the SEC to gain access in a timely fashion to information and data that it otherwise may not receive, thereby further enhancing our ability to identify fraud and root out wrongdoing. I commend you for your inclusion of this important investor protection provision in the Dodd-Frank Act.

Sincerely,

A handwritten signature in black ink that reads "Mary L. Schapiro". The signature is written in a cursive, flowing style.

Mary L. Schapiro
Chairman