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COMMITTEES:
APPROPRIATIONS
BUDGET
HEALTH, EDUCATION, LABOR, AND PENSIONS
HOMELAND SECURITY AND GOVERNMENTAL AFFAIRS

United States Senate

WASHINGTON, DC 20510

November 16, 2015

The Honorable Mary Jo White
Chair
Securities and Exchange Commission
100 F Street NW
Washington, D.C. 20549

Dear Chair White:

I write to you today in response to your letter of July 13, 2015 regarding the volume of stock buybacks. Your letter outlined the limits of trading data available to the Commission for analyzing stock buybacks. You also explained what enforcement actions the Commission takes to prevent stock manipulation generally, but failed to respond to my concerns about the Commission's current rules surrounding issuer share repurchases and the potential for abuse in that space. You also made clear that exceeding the 10b-18 buyback safe harbor in and of itself is not a violation of securities laws. However, I received little explanation of the steps the SEC is taking to enforce the broader anti-manipulation provisions of securities laws with respect to buybacks.

I remain concerned that decision-making on Wall Street and in C-suites across the country is influenced by the fact that a large percentage of an executive's compensation is stock-based, with his or her gains being dependent on boosting the company's stock price, hitting earnings-per-share targets, or both. The prevalence of stock-based pay could be encouraging executives to favor stock-price inflation over productive investments.

This mode of resource allocation is different from the 'pump and dump' fraud you mention in your letter, and it has far more serious implications both for financial markets and for our economy. As Blackrock CEO Larry Fink wrote earlier this year in a letter to CEOs, "the effects of the short-termist phenomenon are troubling both to those seeking to save for long-term goals such as retirement and for our broader economy. In the face of these pressures, more and more corporate leaders have responded with actions that can deliver immediate returns to shareholders, such as buybacks or dividend increases, while underinvesting in innovation, skilled workforces or essential capital expenditures necessary to sustain long-term growth." Indeed, by spending on buybacks to inflate stock prices artificially, executives may be harming investment in the company's capability to generate product revenue, with serious consequences for the long-term earnings of defined-benefit pensions, defined-contribution accounts, and educational endowments.

I remain seriously concerned with the scope and extent of share buybacks and their potentially manipulative effect on short-term share prices and your previous response did not sufficiently explain what the SEC is doing to respond to the buyback phenomenon. Accordingly, I request that you respond to the following questions:

- What steps are you taking to investigate the risk that share buybacks could be manipulating stock prices?
- Have you opened any investigations into specific questionable[1] buyback practices?
- Given that you have explained that the Commission lacks the necessary data to perform analysis on buybacks, are you working to improve your data collection efforts?

In the interest of better understanding the causes and effects of the buyback phenomenon, I also request that the Commission improve its data collection in two significant ways. First, the SEC should mandate daily disclosure by issuers of the stock they have repurchased—including the amounts purchased and the prices paid. Second, the SEC should require annual disclosures of the performance metrics used by a firm to compensate its executives—including specific information on stock-based metrics, such as earnings-per-share.

There are several reasons I believe this disclosure is necessary. As the agency responsible for fair and efficient capital markets, the SEC needs this information in order to assess the adequacy of existing rules on buybacks for regulating manipulation of the stock market. The public interest is also served by learning more about what incentive structures exist for executives making capital allocation decisions. Finally, daily disclosure would bring U.S. financial regulatory policy into line with requirements in other large financial centers such as the United Kingdom, Japan, and Hong Kong. [2]

The overarching reason I am interested in buybacks is that I am concerned that they come at the expense of the investments in innovation, research, and workers that are necessary for stable and equitable economic growth, as some academic studies have suggested. [3] I am not alone. Prominent members of the business community have expressed concerns about the influence that pay based on stock-price levels and earnings-per-share targets can have on an executive's decision-making.[4, 5]

I would like to enlist the SEC as a partner in understanding the effect that the growth of stock-based executive compensation and short-term thinking may have on corporate resource allocation. I do not believe my concern is a partisan one, as it has been echoed in recent months by two SEC Commissioners of both political parties. [6, 7]

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[1] Lazonick, William 'McDonald's Has to Do More than Manipulate Its Stock Price,' *Harvard Business Review*. 14 May 2015.
[2] Kim, Jaemin, Ralf Schremper, and Nikhil Varaiya. "Open Market Repurchase Regulations: A Cross-Country Examination". *Corporate Finance Review*. Jan/Feb 2005.
[3] Lazonick, William. "Stock Buybacks: From Retain-and-Reinvest to Downsize-and-Distribute," Brookings Institution Center for Effective Public Management, April 2015; see also William Lazonick. "Profits without Prosperity," *Harvard Business Review*, September 2014
[4] Barton, Dominic. "Capitalism for the Long Term." *Harvard Business Review*. 01 Mar. 2011.
[5] Fink, Larry. "Focus on Delivering Long-term Value." *Business Insider*. 14 Apr. 2015
[6] Stein, Kara. "Toward Healthy Companies and a Stronger Economy: Remarks to the U.S. Treasury Department's Corporate Women in Finance Symposium." 30 Apr. 2015.
[7] Gallagher, Daniel. "Activism, Short-Termism, and the SEC: Remarks at the 21st Annual Stanford Directors' College." 23 June 2015.

There are growing voices from both inside and outside the investing community who see buybacks as an abdication of corporate leadership at best and a misallocation of resources at worst. [8] And while institutional investors have led this fight, this issue should give pause to anyone concerned with the performance of the U.S. economy. If we are more concerned with artificially inflating stock prices than we are with the hard work that is required for real growth, then future generations will endure a less prosperous American economy.

Sincerely,

Tammy Baldwin
United States Senator

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[8] Farrell, Maureen. "Goldman Sachs to CEOs: Stop Buying Back Stock. Buy Companies Instead." *Wall Street Journal*. 1 June 2015.