

United States Senate

WASHINGTON, DC 20510

June 28, 2018

The Honorable Jay Clayton
Chair
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Dear Chair Clayton:

We write with concerns about the accelerating pace of stock buybacks in U.S. capital markets. The Securities and Exchange Commission (“SEC” or “the Commission”) last updated Rule 10b-18, which governs stock buybacks, in 2003.¹ Since that time, there have been significant changes in executive compensation practices, shareholder activism, and investing technology. Therefore, we respectfully request that the Commission begin a process to review how companies are conducting buybacks under Rule 10b-18 and whether corporate insiders are exploiting buybacks to sell shares received as executive pay at inflated prices.

As you know, Rule 10b-18 was adopted in 1982 to provide issuers a safe harbor protection from claims of market manipulation when repurchasing their stock. This change led to a dramatic increase in stock buybacks. Prior to the rule, in 1981, New York Stock Exchange listed companies spent approximately \$3.5 million, or 2 percent of their profits, on buybacks.² Between 2004 and 2013, America’s largest companies spent \$3.4 trillion on stock buybacks, representing 51 percent of their profits.³ Since the passage of the President’s tax bill in December 2017, publicly-traded U.S. companies are on pace to buy back \$1 trillion worth of their own shares in 2018 alone.⁴ The explosion of stock buybacks has funneled corporate profits to wealthy shareholders and corporate executives instead of workers and long-term investments that spur sustained economic growth.

While we are troubled by the magnitude of stock buybacks and the consequences for employees and communities, we are even more disturbed by the dramatic increase in stock sales by corporate insiders following the announcement of a buyback. This phenomena means it is imperative that the SEC revisit the evolution of Rule 10b-18 to ensure that corporate executives are not using the rule inappropriately to enable advantageous sales of their own stock while ignoring the needs of their companies’ workers.

¹ Securities and Exchange Commission, Final Rule: Purchases of Certain Equity Securities by the Issuer and Others, Release Nos. 33-8335, 34-48766, 17 C.F.R. Pt. 228 *et seq.*

² Williams, Winston, “Corporate America Buys Itself Back,” *New York Times*, 17 Aug 1986.

³ Lazonick, William, “Stock buybacks: From retain-and-reinvest to downsize-and-distribute,” Center for Effective Public Management at Brookings, April 2015. <<https://www.brookings.edu/wp-content/uploads/2016/06/lazonick.pdf>>

⁴ Wang, Lu, “Record Buybacks Put Shareholder Payouts on Pace for \$1 Trillion,” *Bloomberg*, May 17, 2018. <<https://www.bloomberg.com/news/articles/2018-05-17/record-buybacks-put-shareholder-payouts-on-1-trillion-pace>>

Commissioner Robert Jackson recently published a study that demonstrated the percentage of insiders selling shares more than doubled immediately following their companies' buyback announcements. Commissioner Jackson's analysis of 385 firms that announced buybacks from 2017 to Q1 2018 shows that, "[d]aily stock sales by the insiders rose from an average of \$100,000 before the buyback announcements to \$500,000 after them. The sellers received proceeds totaling \$75 million more than had they sold before the announcement [and at] 32% of the companies, at least one insider sold in the first 10 days after the buyback announcement."⁵ Put another way, immediately after the company's executives signal to investors that the stock is undervalued (and subsequently boost the stock an average of 2.5 percent)⁶ these same executives cash out their shares, which are intended to incentivize them to manage the firm for the long-term.

Commissioner Jackson is not the only member of the Commission who supports a review of 10b-18. Commissioner Hester Peirce agreed during her confirmation process that a review of Rule 10b-18 would be "timely" given the increase in buyback activity, adding "I look forward to working with my fellow Commissioners and the SEC staff to look at the evidence about how and why buybacks are occurring and assess whether, in light of this evidence, changes to the regulatory framework are needed."⁷ Similarly, at a Senate Banking Committee hearing last year you noted, "one thing that does trouble me is if these stock buybacks are motivated not by the long-term interest of the company but some short-term interest."⁸

We, too, are concerned that short-term interests are too often driving stock buybacks. Shareholders, employees, and the American public will benefit when executives have the appropriate incentives to facilitate job growth and long-term investment in their firms. Accordingly, it is time for the public to weigh in on the impact of the buyback phenomenon on ordinary investors, wages, investment, and the overall competitiveness of U.S. companies.

To that end, we ask you to open a public comment period to review the SEC's current rules around share repurchases. Last year, you solicited public comment prior to proposing an updated fiduciary standard. In your public statement, you justified opening the public comment period by noting the "significant developments" in the marketplace since 2013, when the Commission had last solicited input from the public. As stated above, we believe the developments in executive compensation, shareholder activism, and buyback activity warrant serious reconsideration and review of Rule 10b-18.

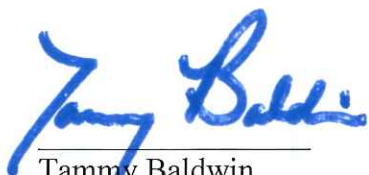
⁵ Morgenson, Gretchen and Tom McGinty, "Insiders Pocket Gains on Buybacks, Vexing Regulator," *The Wall Street Journal*, June 10, 2018. <<https://www.wsj.com/articles/insiders-pocket-gains-on-buybacks-vexing-regulator-1528646400>>

⁶ Jackson, Robert J., "Stock Buybacks and Corporate Cashouts," Remarks as prepared for delivery at the Center for American Progress, June 11, 2018.

⁷ Peirce, Hester. "Response to Senator Tammy Baldwin." 8 Dec 2017

⁸ United States Senate Banking Committee, "Hearing on the Securities and Exchange Commission," September 26, 2017.

Sincerely,



Tammy Baldwin
United States Senator



Chris Van Hollen
United States Senator



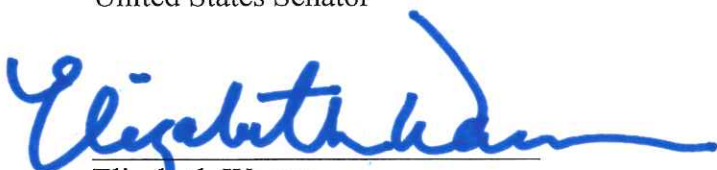
Charles E. Schumer
United States Senator




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United States Senator



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United States Senator



Elizabeth Warren
United States Senator



Ron Wyden
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Mark Warner
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Sheldon Whitehouse
United States Senator



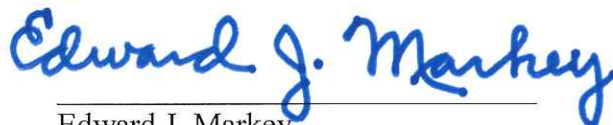
Kirsten Gillibrand
United States Senator



Jack Reed
United States Senator




Richard Blumenthal
United States Senator



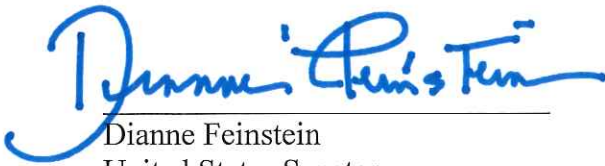
Edward J. Markey
United States Senator



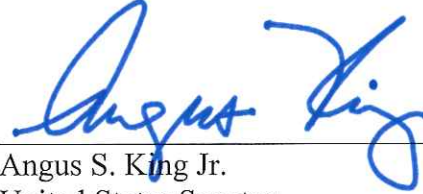
Mazie K. Hirono
United States Senator



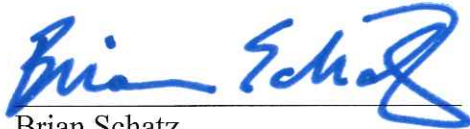
Benjamin L. Cardin
United States Senator



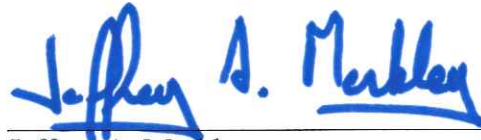
Dianne Feinstein
United States Senator



Angus S. King Jr.
United States Senator



Brian Schatz
United States Senator



Jeffrey A. Merkley
United States Senator



Joe Donnelly
United States Senator



Margaret Wood Hassan
United States Senator

cc: The Honorable Kara Stein, Commissioner
The Honorable Michael Piwowar, Commissioner
The Honorable Robert Jackson, Commissioner
The Honorable Hester Peirce, Commissioner