

Presidential Working Group Issues Recommendations to Protect U.S. Capital Markets

AUGUST 12, 2020

On August 6, 2020, the President’s Working Group on Financial Markets^[1] (PWG) announced its report on “Protecting United States Investors from Significant Risks from Chinese Companies” to the White House, making five recommendations “designed to address risks to investors in U.S. financial markets” posed by countries in non-cooperating jurisdictions (NCJs), including China, that do not require registration with the Public Company Accounting Oversight Board (PCAOB) or compliance with U.S. securities laws. The recommendations follow President Trump’s June memorandum to the PWG to review and make recommendations with respect to the Chinese government’s actions to prevent Chinese companies from complying with U.S. investor protection regulations and are informed by the Holding Foreign Companies Accountable Act, which passed the Senate in May 2020.

The Recommendations

The PWG recommendations are directed principally to the SEC, and SEC Chairman Clayton has directed the SEC staff to prepare proposals in response to the recommendations.

ITEM

DESCRIPTION

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Enhanced Listing Standards for Access to Audit Work Paper	<p>Enhancing the listing standards of U.S. securities exchanges to require, as a condition to initial and continued exchange listing:</p> <p>(a) PCAOB access to work papers of the principal audit firm for the audit of the listed company; or</p> <p>(b) if the company is unable to provide such access as a result of governmental restrictions in NCJs, providing a co-audit from an audit firm with comparable resources and experience where the PCAOB determines it has sufficient access to audit work papers and practices to conduct an appropriate inspection of the co-audit firm.</p> <p>Note: The PWG recommends a transition period until January 1, 2022 for currently listed companies from NCJs to come into compliance in order to reduce market disruption. These new standards would apply immediately to newly listed companies, once effective.</p>
Enhanced Issuer Disclosures	<p>Requiring enhanced and prominent issuer disclosures of the risks of investing in issuers from NCJs, including on issues such as corporate structure, the risks related to a lack of enforcement mechanisms in the NCJ's regulatory environment, and non-compliance with PCAOB inspection requirements.</p> <p>Note: The PWG recommends that the SEC issue interpretive guidance to clarify these disclosure requirements to increase investor awareness and general awareness of the risks of investing in such companies.</p>
Enhanced Fund Disclosures	<p>Reviewing the risk disclosures of registered funds that have exposures to issuers from NCJs to enhance the disclosures by these funds.</p> <p>Note: The PWG recommends that the SEC issue interpretive guidance to clarify the disclosure requirements to increase investor awareness of the risks of investing in such funds.</p>
Greater Due Diligence of Indexes and Index Providers	<p>Encouraging or requiring registered funds that track indexes to perform greater due diligence on an index and its index providers, prior to the selection of the index to implement a particular investment strategy or objective. The PWG noted that enhanced due diligence could "result in index providers more carefully considering the implications of different regulatory, accounting, auditing and financial recordkeeping standards when considering issuers to include in an index."</p>

ITEM	DESCRIPTION
Guidance for Investment Advisers	The PWG recommends that the SEC issue guidance to investment advisers with respect to fiduciary obligations when considering investments in NCJs, including China. This guidance is expected to “result in additional investigation into the risks and regulatory implications of investments in China and other NCJs.”

Please see our blog [post](#) from June 18, 2020 with additional background information on the growing call for stricter securities law enforcement of companies from NCJs. Capital Markets & Securities Law Watch will continue to monitor any developments on these recommendations, including any SEC proposals, and provide updates to our readers.

[1] The Presidential Working Group is comprised of the Secretary of the Treasury, the Chairman of the Board of Governors of the Federal Reserve System, the Chairman of the Securities and Exchange Commission, and the Chairman of the Commodity Futures Trading Commission.

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