2018 CLM Annual Conference
March 14-16, 2018
Houston, TX

Fake News or Grim Reality? Trump, the SEC, DOJ, DOL, and Predicted Effects on Business and Insurance

I. First Year of the Trump Administration in Review

A. The Predictions

The 2016 presidential election results were a surprise to most which led to immediate and dire predictions about many things including the economy as a whole, the stock market, and radical changes in various agencies within the federal government. While there have been unprecedented and unexpected developments in many areas under the control and direction of the White House, some of the predicted changes have not occurred or at least have not yet become apparent.

A few of the predictions:

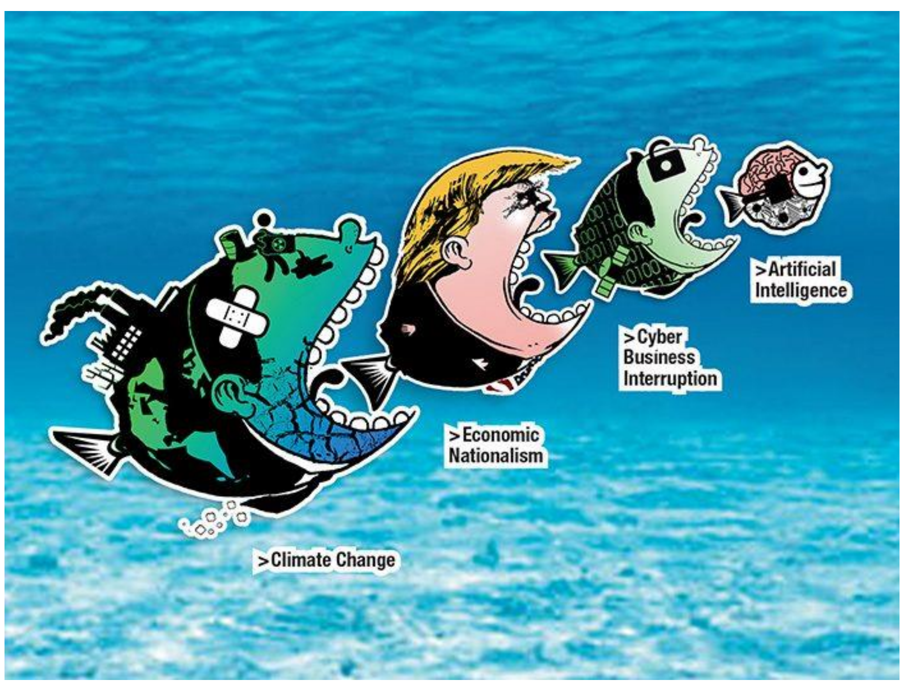
- U.S. GDP will stagnate in 2017 with growth over 5 years 4.7% less than previously forecast due to unsustainably high tax cuts raising the deficit and protectionist and anti-immigrant policies raising costs for businesses and consumers. (*Euromonitor International*, October 7, 2016.)
- The election could "presage a longer slump" if investors believe uncertainty will harm growth and corporate profits. Expect volatility and wobbly bond prices. Expect dramatic tax cuts to benefit the rich with a large increase in the deficit, a challenge to the role of the Federal Reserve, loss of health insurance for millions, more vulnerability for undocumented immigrants, and darkening of the outlook for global trade growth. (*The Economist*, November 9, 2016.)
- 10% drop in global markets predicted in the event of Trump victory. (*Forbes*, November 10, 2016, referencing pre-election predictions by Dartmouth and MIT/IMF economists.)
- "Inaccurate prognostication" about the near-term market effects of a Trump victory suggests modesty is in order with respect to the ability to predict how his policies will play out. Market suggests that investors thought the positive effects of the Trump agenda—lower taxes on business, fewer regulations, infrastructure spending, and growth in corporate profits—would happen but the approach to potentially negative policies—abandoning trade agreements,

deportation of immigrants—might be more cautious. ("The Upshot", *The New York Times*, November 12, 2016.)

- EPA will roll back regulations making it easier to drill in the U.S. with mixed impact—good for Big Oil but bad for already glutted oil markets (CNN, November 16, 2016.)
- Dodd-Frank will not be repealed but there will be some targeted rollback. Broadest impact on financial regulation will come from appointments. SEC will not complete asset manager rules. DOL fiduciary rule will remain but compliance deadlines will be delayed. Anti-money laundering and sanctions regulation will stay the course. ("First take," PwC, November 17, 2016.)
- Impact on the housing market due to higher interest rates/mortgage costs, deportation effect on labor costs, freer markets, lower taxes, and the "wealth effect." (*TheStreet*, December 10, 2016.)
- FCC will reconsider net neutrality. (*The Mercury News*, December 29, 2016.)
- Sectors that will thrive under Trump in 2017 are energy, financials, industrials, and materials. ("3 Sectors That Will Win Under Trump In 2017," *Forbes*, February 6, 2017.)

Notably, a lengthy post-election Washington Post article identified potential effects on 15 industries without mentioning the insurance industry at all. (*The Washington Post*, November 12, 2016.) Of course, the industries predicted to be impacted would have a potential ripple effect on the insurance industry, *e.g.* oil and coal, infrastructure, banks, brokers, health care including pharmaceuticals, media, Silicon Valley, etc.

As an interesting corollary, "2017 Most Dangerous Emerging Risks" as identified by Risk & Insurance, did not even mention Trump by name although he is entertainingly depicted in a caricature as part of the article's lead graphics. (*Risk & Insurance*, April 2017.)



The article suggested five emerging risks that could cause “massive losses for commercial insureds and carriers”:

1. Climate change resulting in sea rise which could “wreck coastal real estate values”
2. Economic nationalism, domestically
3. Economic nationalism, globally
4. Layered risk due to use of artificial intelligence in manufacturing and other processes
5. Threat that hackers “could take down the internet” resulting in “massive cyber business interruption.”

While the article never mentions Trump by name, the anticipated impact of his administration is linked to protectionism as a threat to “supply chains and the free flow of commerce.” (*Risk & Insurance, supra.*) Looking back at the end of 2017, a link to each of the emerging risks identified by *Risk & Insurance* in April can be found in the policies (or lack thereof) of the Trump administration.

What is clear about the pre- and immediately post-election predictions is that very few of them focused directly on potential impacts to the insurance industry other than in the health care context. Broad market predictions and those relating to corporate impact, *i.e.* impact to commercial insureds, had to be interpreted to reflect on insurance industry consequences from the election.

B. What Actually Happened in The Stock Market

After an initial drop in premarket trading with major indexes down 2.5% (Dow futures were down more than 800 points), literally within hours of the election the market opened flat and then closed up 1.11-1.4% depending on the index. (*Forbes, supra*.) The following week, the S&P 500 index was up nearly 4%. (*The New York Times*, November 12, 2016.) Since those early days, the market has continued to rise—S&P 500 up 23%, Dow Jones up 30%, NASDAQ up 31%. (“Stock Market Results: Early Trump vs. Early Obama,” *Cabot Wealth Network*, December 12, 2017.) While these results are similar to those of the first Obama year in office, Trump started “amid almost universal growth” while Obama was elected “in the midst of the greatest economic downturn” since the Great Depression. Putting aside the comparison, “the daily noise projecting Trump’s poisonous effect on stocks is not only overstated; it’s simply incorrect.” (*Cabot, supra.)*

C. What Actually Happened with Securities Suit Filings

While there were major changes in the Securities & Exchange Commission in 2017, it will take time to see if changes in investigations and enforcement result in fewer securities filings in the future. 2017 actually saw the highest number of securities lawsuit filings since 2001. Early estimates by Kevin LaCroix of the *D&O Diary* reflect a 120% increase in 2017 securities lawsuit filings over the 1995-2015 average number of filings. (“Securities Suit Filings at Historically High Levels During 2017,” D&O Diary, January 1, 2018.) Although there was an overall increase in filings, the number of securities lawsuits decreased in each quarter of the year which could indicate a downward trend. Life sciences companies including pharmaceutical and medical device companies accounted for nearly 20% of the filings. Computer-related companies represented just under 8% of the filings with banking following close behind at 6%.

D. Actual Impacts on Federal Agencies

1. Securities & Exchange Commission (SEC)

Changes at the SEC started with a new Chair, former Sullivan & Cromwell partner Jay Clayton. At his confirmation hearing, Clayton asserted that he is "100 percent committed to rooting out any fraud and shady practices in our financial system." Two months later at the Economic Club of New York on July 12, 2017, he affirmed the mission of the SEC—investor protection, maintenance of fair, orderly and efficient markets, and facilitation of capital formation—and said that to determine the SEC's success its analysis should focus on the long term interests of Main Street investors, "Mr. and Mrs. 401(k)."

What has Chairman Clayton's SEC done since he assumed control? He has indicated his concerns about Internet Coin Offerings ("ICOs") and seems likely to pursue unprepared participants in the ICO world with SEC investigations, regulations, and prosecutions. He has cautioned that many ICO platforms are "susceptible to manipulation and other fraudulent practices by ICO insiders, management, and better-informed traders." ("The SEC and ICOs: Winter is Coming," *D&O Diary*, November 14, 2017.)

Other than pursuing fraud and manipulation in the world of ICOs, SEC enforcement activity in general under the new administration has waned with fewer enforcement actions and reduced financial penalties. For the fiscal year ending September 2017, there was a 17.6% drop in primary and follow-on enforcement actions. There was also a 15.5% drop in the amount of fines collected. Enforcement actions against public companies were reduced by a third. When separated into the first half of the fiscal year (Obama) and the second half (Trump), SEC actions against public companies went from 45 to 17 and settlements fell from $1 billion to $196 million. ("SEC Enforcement Activity Plunged With Dawn Of Trump Era," *Law360*, November 14, 2017.) These numbers vary slightly as reported in the D&O Diary, but there is agreement that the number of enforcement actions against public companies is down significantly since the Trump appointees have assumed control. ("SEC Fiscal Year Enforcement Statistics Reflect an Agency in Transition," *D&O Diary*, November 26, 2017.) There is also agreement that it is too soon to know whether these declines are due to changes in SEC leadership, "a drier pipeline of cases, or a broad policy shift in the enforcement program."

While the number of SEC enforcement actions has declined, the Whistleblower Program continues to grow. ("SEC Whistleblower Program Continues to Surge," *D&O Diary*, November 26, 2017.) As reported in the D&O Diary, the number of whistleblower reports increased again in FY 2017, as it has every year since the program's inception in FY 2012, to 4,484 reports, an increase of about 6.3% over the prior year. This included reports from all 50 states, the District of Columbia, and 72 different countries.

2. Department of Justice (DOJ)

The changes in leadership and the impacts on the DOJ have been well and almost continuously documented in the press since Jeff Sessions assumed the role of Attorney General.

It would be an understatement to note that it is certainly not business-as-usual at the DOJ which is illustrated by an assertion from the DOJ in federal court that Trump's tweets are "official statements of the President of the United States." In a second case, the DOJ stated that while the tweets are official policy statements, the president's actions with his Twitter account are "personal conduct that is not an exercise of state power." The DOJ further argued that "the fact the President may 'announce actions of the state' through his Twitter account does not mean that all actions related to that account are attributable to the state." ("DOJ says Trump's tweets are official presidential statements," *ABA Journal*, November 14, 2017.) Is it any wonder that lawyers are accused of doublespeak?

More substantively, the DOJ through Deputy Attorney General Rod Rosenstein has addressed the administration's position on individual accountability for corporate wrongdoing. While acknowledging that past practices should be periodically reviewed, Rosenstein generally supported the principles of the Yates memo stating that "prosecutors should be cautious about closing investigations in return for corporate payments without pursuing individuals who broke the law." ("Deputy AG Emphasizes Continued Individual Accountability for Corporate Misconduct," *D&O Diary*, October 31, 2017.) Common themes to watch will be the DOJ's "resolve to hold individuals accountable for corporate wrongdoing," "the government should not use criminal authority unfairly to extract criminal penalties," and changes to "make the policy more clear and concise." (*Id*.)

The DOJ has also made it clear that it intends to continue the Obama-era bribe enforcement policy with some modifications. Previously, DOJ considered reducing financial penalties for companies that "came clean" with respect to bribes. The "new" DOJ "will be more likely to consider forgoing criminal charges as well." ("Companies Get Extra Incentive to Disclose Bribes: No Charges," Bloomberg, November 29, 2017.) Again it was Rosenstein who announced the expansion of the prior policy as part of the new guidelines for enforcing the Foreign Corrupt Practices Act which prohibits payments to foreign officials to obtain or retain business. Rosenstein has stated that criminal charges may be avoided if companies cooperate "with prosecutors, fix the problem, and help prosecutors find those responsible for the misconduct." (*Id*.)

Separate but certainly related and relevant to the DOJ is the record-breaking rate at which the Trump administration is successfully nominating and filling open positions within the federal judiciary. As of November 11, 2017, Trump had appointed one Supreme Court Justice and eight appellate court judges. Almost all of the nominees have been men. ("Trump Is Rapidly Reshaping the Judiciary. Here's How." *The New York Times*, November 11, 2017.) As of December 15, 2017, he had appointed a total of 12 appellate judges. ("President Trump Appointed Four Times as Many Federal Appeals Judges as Obama in His First Year," *Time*, December 15, 2017.)

3. Department of Labor (DOL)

As one practitioner in the labor and employment arena has observed, the DOL did not necessarily eliminate regulations in 2017 but has transformed itself from an enforcement agency to an educational agency. Some pronouncements from the DOJ will clearly have an effect on DOL such as Attorney General Sessions' reversal of prior policy protecting transgender workers under Title VII.

The agency will clearly be impacted by its new Secretary, R. Alexander Acosta, a pedigreed government veteran with a specialization in labor and employment issues and the support of employer groups. Acosta indicated early in his tenure that DOL would follow the president's directive and review the fiduciary rule which required advisers to act in the best interests of their clients and put their clients' interests above their own. He also stated that DOL would review and possibly revise the overtime rule initiated by President Obama. ("5 key facts about the new DOL secretary," *Employee Benefit News*, April 27, 2017.) More recently, at a House Education hearing, Acosta stated that although DOL may be postponing implementation of some fiduciary rule compliance rules and procedures, "it still expects retirement advisors to provide impartial advice, and to act in the best interests of the consumers." He further noted that the fiduciary rule is in effect and that the DOL's Employee Benefits Security Administration "has the tools it needs to address material, willful violations of the standards." ("Advisors Must Act in Customers' Best Interest: DOL Secretary," *ThinkAdvisor*, November 16, 2017.)

The Equal Employment Opportunity Commission (EEOC) is also likely to transform as Trump makes his appointments to the five person commission but the administration has been slow to appoint new commissioners and there is one vacancy. Meanwhile, EEOC filings were up in 2017 with Chicago, Texas, Philadelphia, and Los Angeles identified as "hot spots."

E. Resulting Impact on Insurers and Insureds

It really too soon to see the real impacts of the first year of the Trump administration on the insurance industry. While one can see the changes noted above, the impacts on insureds are just beginning to materialize.

II. The Future—2018 and Beyond

One definite hallmark of the Trump presidency is uncertainty which is, of course, not a favored concept in the insurance world. As noted above, this uncertainty has surprisingly not, at least not yet, had a negative impact on the stock market. Even so, identifying trends and making predictions and forecasts in the Trump era is dicey business. Based on 2017, there are some areas for which 2018 changes and impacts seem likely.

A. Trends, Predictions, and Forecasts for Federal Agencies

1. SEC

SEC officials have stated that the agency will "pivot away from the prosecutorial approach" and will drop the "strategy of pursing many cases over even the smallest violations." Enforcement priorities will be guided by five "core principles…focus on the Main Street investor; focus on individual accountability; keep pace with technological change; impose sanctions that most effectively further enforcement goals; and constantly assess the allocation of resources." (*D&O Diary*, November 26, 2017, *supra*.) So while the number of enforcement actions against public companies may continue to decline, the focus on individual accountability in those actions will remain strong. The creation of a Cyber Unit will focus on new and the greatest risks facing the securities markets.

It is too early to tell for sure if new leadership will continue to fund the Whistleblower Program but there have not been any indications that the program will be abandoned. To the contrary, the agency's FY 2017 report includes a significant section on "its efforts to battle actions taken in retaliation against whistleblowers" as well as employers' actions to "interfere with individuals' ability to report potential wrongdoing to the SEC." Further, since the program has led to nearly $1 trillion in recoveries, it is likely to survive. (*Id.*)

Another key area to watch is potential deregulation, particularly with respect to changes to Dodd-Frank. A February 3, 2017 Executive Order requires the Treasury Secretary to review existing laws and regulations. Targeted reform is expected rather than full repeal. Smaller financial institutions are likely to see more immediate relaxation of supervisory requirements.

2. DOJ

Although the DOJ has also reinforced its commitment to pursuing individual accountability for corporate wrongdoing and individuals will clearly continue to face the possibility of direct personal liability, the specifics of this policy under the new administration are not yet clear. Will the cooperation requirement—corporations must provide DOJ relevant facts about individuals involved in misconduct to receive credit for cooperation—continue to be part of the policy? Even this one point could have major implications as discussed more fully below. What Deputy AG Rosenstein has made clear is that he believes that policy should not be set forth in AG memos but rather in the U.S. Attorneys' Manual. (*D&O Diary*, October 31, 2017, *supra*.) This may be the document to watch for changes as 2018 progresses. (*See also*, *Bloomberg*, November 29, 2017, *supra*.)

Given the number of vacancies across the federal judiciary due to a slowdown of nomination hearings during the Obama administration, the pace of judicial appointments from the Trump administration is likely to continue at a breakneck pace. This is one of the few things that the new administration is doing quietly and, for the most part, under the radar and yet it may very likely be the most transformative and enduring impact of the Trump era.

3. DOL

The DOL has drafted regulations describing how it would enforce the best-interests standards of the fiduciary rule and the draft is under review by the Office of Management and Budget. Secretary Acosta has stated that companies would get an extension that would give them at least 18 months to come into compliance with the remedy requirements. (*ThinkAdvisor, supra*.) Other topics of interest to employee benefits financial advisors identified by Acosta as under review at DOL are efforts to help employees with disabilities and to hold down the costs of health benefits.

Other changes at DOL and related agencies could have significant changes for 2018 and beyond. Watch for new appointments at the EEOC, possible changes in policies related to sexual orientation, retaliation claims, and pay equity, and heightened focus on harassment in the workplace.

B. Trends, predictions, and forecasts for the insurance industry

As noted at the outset, although there have been many changes in the first year of the Trump administration, the impacts on the insurance industry have been largely indirect other than in the health care arena. That is not to say that the financial impacts will not be significant. The increased number of securities lawsuit and EEOC filings in 2017 are pretty clear indicators that claim costs in the management liability will continue to increase. If the DOJ follows through on its stated commitment to pursuing individual accountability for corporate wrongdoing, this will also contribute to the increasing claim costs for insurers.

It is too early in the Trump era to know if the changes in policies and regulations will have significant impacts on insurance markets. While the stock market goes up and down every day, the insurance markets adjust in a much more measured fashion. It that regard, even 2018 is unlikely to reveal any major changes to the insurance industry other the obvious changes in the health care market. What *can* be seen very clearly even at these early stages of the Trump administration is that the transformation of the federal judiciary will be profound and have broad and lasting ramifications across sectors and industries. How the “new” federal judiciary and sweeping changes in policies including deregulation will impact the insurance industry and its customers will be fascinating to watch in 2018 and beyond.