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RESPONSIBLE DEREGULATION

Remarks of
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RESPONSIBLE DEREGULATION

It's hard to pick up a newspaper these days without finding some reference to deregulation. There's a great movement in this country now to re-examine the relationship between government and business, and to revamp our Nation's regulatory philosophy, that is, the means by which we seek to insure that business is responsive to a broad range of social concerns. Deregulation is one of the themes on which the new government was elected, and promises to be one of its early priorities. Given the importance of this movement to the future of our economy, and given that the Securities and Exchange Commission is right in the thick of it, I thought I would share with you today some of my initial thoughts on deregulation.

Initially, it seems to me important to clarify just what we mean by "deregulation." I expect the meaning of that term will vary from one substantive area to another. In the case of the securities markets, we really are <u>not</u> talking about the removal of regulatory restrictions across the board, but rather about a reorientation -- an effort to accomplish our basic goals, but by placing as little burden as possible on legitimate business. Remember that the essential goal of the SEC is to assure economically efficient and smoothly functioning securities markets, by encouraging full disclosure, preventing fraud and manipulation, and maintaining a high degree of business ethics throughout the securities markets. Unlike regulation in many other fields, these goals represent

not an interference with the forces of the free market, but an effort to keep the markets functioning close to their theoretical ideal. Accordingly, these goals are as valid today as when the SEC was first established in 1934. It's the methods that are now under scrutiny.

I fully support the Commission's reorientation toward more responsible and less intrusive regulation. My support is long-standing and grows out of my first-hand experience. As many of you know, before joining the Commission, I worked for over a decade as a securities lawyer, facing the many challenges that confront those who seek the capital to build and expand American business. Sometimes -- too often, in fact -- I found more than challenges. I found obstacles: governmentally-imposed requirements and prohibitions that were, I felt, quite unnecessary, and that only added to the cost of a given transaction without adding a commensurate degree of investor protection. I also found many areas where the boundaries of the law were unnecessarily clouded, so that legitimate commercial transactions -- which could have generated the jobs and production facilities America so badly needs -- were abandoned because business people were afraid to proceed in the face of legal uncertainty. Therefore, I come to the SEC determined to press the agency to continue to rationalize and simplify and, where appropriate, to eliminate the welter of rules that I feel are weighting down American business today.

Nevertheless, I also find that many of the criticisms

that are voiced about the regulatory process today are not always well-informed or well thought out criticisms. Frequently critics are overbroad in their assumption that all regulatory agencies have the same problems or attitudes. In the same vein, some of the so-called "reform" proposals that have been put forward are simply not workable.

The Commission, as you may know, has had for some years an active program to re-examine and revamp out-dated and overly burdensome regulations. In the past couple of years, we've broadened substantially the small issuer exemptions from '33 Act registration, simplifying their use and increasing the maximum dollar amount of securities a company can offer to the public without registration. For registered public companies, we are integrating the '33 Act and '34 Act disclosure requirements, and introducing a system of continuous registration. We've made it easier to resell privately-place securities; alleviated the plight of inadvertant investment companies; and simplified the problems of public utilities that wish to become joint owners of a generating subsidiary.

Speaking from the vantage point of the SEC's experience, my remarks today will be addressed primarily toward the wisdom of many of the present proposals for regulatory reform. I'm sure you are familiar with many of these initiatives: the Bumpers Amendment, which would alter the burden of proof when agency regulations are challenged in court, so as to undercut the agency's ability to rely on its own substantive expertise in the area it regulates; the Regulatory Flexibility Act, already law, which requires

all agency rulemaking which would have significant economic impact on a substantial number of small entities to be accompanied by preliminary and final published statements of the impact of the rule on small business and the reasons the agency has rejected possible alternatives; the Paperwork Reduction Act, also now law, which requires an agency to obtain OMB approval for any forms the agency wishes the public to fill out, whether public compliance is mandatory or voluntary; the one- and two-house legislative veto of agency rulemaking, which would allow Congress to override new agency rules by the vote of one or both houses acting without Presidential concurrence; and the various proposals to require detailed cost-benefit analyses to be made before new rules can be issued.

At best, these bills and proposals add very little to the ability of a capable agency that is already determined to press forward with deregulation. But, if this were their only fault, these proposals would not be worthy of much attention.

Unfortunately, these proposals do more than that. The raft of procedural requirements that these rules impose will actually distract from and undercut our efforts to deregulate responsibly.

These points can best be explored by considering how and why the SEC has made the progress it has toward reducing regulatory burdens. First, <u>why</u> did the Commission get an early start on this problem? It should be obvious that we didn't do it because of the Regulatory Flexibility Act, or OMB review, or the Bumpers Amendment. I say "obvious" because the Commission began its initiatives at a time when these items were at best

no more than mere murmurings.

Then why did we do it? The most important reason is simply that we share with the industries and professions we regulate, and with the investors we protect, a strong commitment to maintaining healthy capital markets.

This commitment pervades the entire history of the Commission. The SEC grew out of the market collapse of 1929, and out of the widely-shared public perception of the early 1930's, that the markets were not fair and honest, and that a person was better off to keep his money at home under the mattress. Congress understood in 1933 and '34 that strong business rests upon strong capital markets, and that if citizens were going to take the risk of investing in these markets, they would have to be assured that the game was at least an honest one. So, while we were given extensive powers to regulate and enforce, it was with an understanding that the aim was to strengthen the capital markets. That remains our commitment today, and it's one we take very seriously.

But it's one thing to have a commitment, quite another to be able to carry it into practice. We are doing that, and doing it quite successfully. In my opinion, there are four major reasons for our success.

The first reason for our success is that we maintain an active dialogue with the industries we regulate and the professionals -- primarily lawyers and accountants -- who service those industries.

You may be aware, for example, that in 1976, the Commission

established an Advisory Committee on Corporate Disclosure. This committee brought together a wide range of views of the Commission's work, including some of its most severe critics. The Advisory Committee brought into the foreground a number of proposals to integrate and simplify '33 and '34 Act reporting requirements -- proposals that previously had been merely percolating in the background.

In 1978, the Commission held a series of hearings on the special problems of small business under the Securities Act and the Exchange Act. Commissioners and Commission staff traveled across the country, listening to over 150 speakers in six different cities discuss their concerns in this area.

The Commission heard from these people that the then-existing maximum for the amount of capital small issuers could raise under the exemptions from registration was too low; that certain of the requirements served no useful purpose; and that unnecessary restrictions on resale hurt the market for unregistered securities of small issuers.

We continue to carry on this dialogue with practitioners every year at the annual "SEC Speaks" conference, attended by hundreds of securities lawyers from all over the country. Commissioners and staff members take part in panel discussions with outside atorneys, answer questions from the floor, and generally make themselves available for buttonholing.

On specific issues, we often issue concept releases which are intended to elicit comments from the public. Typically, these releases indicate that we are aware of a certain problem

and are considering various methods for dealing with it. They solicit public comments on these methods, as well as soliciting any other suggestions relating to the problem anyone may have.

These are merely some of the ways we carry on our dialogue. There are many other, less formal channels, too. The important thing is that we understand the need for such a dialogue. We would be the first to say that we have no corner on the market for vital information and new ideas. This is all the more true as we move further and further into areas of deregulation, where there is little concrete experience and no accepted wisdom on how to proceed.

A second reason we've been successful at deregulation is that we have had considerable freedom of action. Our rulemaking has not historically been subject to especially detailed procedural requirements, or to review and second-guessing by other agencies. When we were satisfied, we went ahead.

This is one area in which the so-called regulatory reform proposals will be the most counter-productive. Indeed, there is something ironic about these proposals as an approach to deregulation. They bear a strong family resemblance to the techniques of regulation itself. In years past, we thought we could achieve a vastly better society if only we could specify in enough detail the procedures that every business had to follow in a number of critical areas: what information they had to give their stockholders, how much they could charge their customers, what markets they could enter, and so on. But in the past few years, we've become acutely aware of the limitations of these

regulatory techniques as a means of controlling business. We now understand that they often produce greater emphasis on form than on substance; and that they can stifle creativity and initiative. We realize now that society as a whole pays the price for implementing these regulations, and that the price is sometimes far greater than any benefits we may obtain.

Yet, there are many who are now trying to "regulate" the regulatory agencies into deregulation. They want to specify in minute detail exactly what procedures each agency would have to follow in its rulemaking, what subject matter it would have to consider, and what statements it would have to include in its releases. They want to impose on agency rulemaking a requirement for review by officials in <u>other</u> agencies -- people who in all likelihood will not be as well-informed as the officials of the original agency.

I predict, if these measures are adopted, that we will find in the coming decades, that they are no more useful as a means of controlling government than they are as a means of controlling business. We'll see government officials shuffling even more paper about than they have in the past, with less in the way of substance to show for it. We'll find that we're attacting a lower calibre of intellect to public service; that government is unable to react quickly when it has to; and that, when all is said and done, we've accomplished very little to increase the average government agency's sensitivity to the costs of regulation, or to the burdens it puts on the business community. In short, these approaches are very

much at odds with the freedom of action that I believe is essential to successful deregulation.

A third major reason why the Commission has been successful in its own deregulatory initiatives has been the quality of our staff. We have been indeed fortunate to have attracted to the Commission a cadre of excellent people who share our commitment to make deregulation work. They are creative, hard-working, and -- perhaps most important -- they are excellent managers. They have streamlined the working divisions of the Commission and they produce results, sometimes at a breath-taking pace.

There is a point here that bears considerable emphasis. Responsible deregulation will not happen simply because we all wish it to. It has to be brought into being through a very intensive effort. It's a very sophisticated exercise. It's also a big job. We are currently reconsidering, in just a few years, a stack of rules and interpretations that have been piling up since 1934. We can only do this if we can attract and keep at the agency high-quality people -- bright, hard-working and possessed of good managerial skills.

Once again, this leads me to comment on the many proposals being bandied about today for regulatory reform and governmental cut-backs. Among these proposals are some that almost certainly will hurt the ability of various agencies to attract high quality staff by cramping a manager's ability to make his or her office an exciting and creative place. These proposals may well hinder the effort to achieve balanced deregulation, not help it.

A fourth major reason the Commission has been successful at reducing regulation is that we are well equipped to analyze and manage the risks of deregulating. And please make no mistake about it, there <u>are</u> risks associated with deregulation. In some cases, we may be setting loose forces that have been fenced in for decades, witness the talk of lowering the barriers that the Glass-Steagall Act imposes between commercial and investment banking. In other cases we are giving full rein to activities that didn't even exist in the days before federal regulation, such as the great proliferation of new financial instruments now appearing in the markets. Sometimes, the empirical data we would like to see before we have to go ahead with a given step simply doesn't exist. Certainly there is no exact information on all the many interconnections that lace our economy together.

The simple fact that these risks exist can be a significant barrier to deregulation. Government officials are only human. Like everyone else, we would rather be safe than sorry. And there is always a strong temptation to think that safety lies in the direction of keeping regulated entities on a short leash, as opposed to cutting the leash or even lengthening it.

Breaking through this barrier is a question of personal fortitude as well as good management. We cannot do much about fortitude, you either have it or you don't. But the example of the Commission proves that we can do a great deal to help decision-makers evaluate and manage risk so that they are encouraged to take that uncertain step.

One of the first keys to risk management is a thorough airing of viewpoints. We are quite fortunate at the Commission that our decision-making has always been characterized by vigorous internal staff debate.

The debate in turn is facilitated by the simple fact that we are a Commission -- a collegial body that makes its final decisions at regularly scheduled meetings. The whole staff has access to the calendar of Commission activities. If they object to a given proposal or have a different point of view, they know when to show up for the debate. And believe me, they do show up. By the time we have to vote on difficult issues, we've generally heard a full range of viewpoints put forward by some very skilled advocates. I, for one, feel a good deal more comfortable moving ahead in certain difficult areas because of this debate.

Another key to good risk management is the ability to monitor the results. Obviously, one function of such monitoring is to determine whether your deregulatory initiatives are having the desired consequences -- whether they are targeted in the right areas, and whether they go far enough. Again, we are fortunate to have at the Commission an excellent staff of economists and statisticians in the Directorate of Economic and Policy Analysis, which works alongside the Division or Office proposing a given deregulatory initiative to devise a monitoring program.

More important, though, for ferreting out the risks of deregulation, is a program to alert the agency when there are

unintended consequences of a seriously deleterious nature. These unintended consequences, by their very nature, are difficult to spot. How does one devise a program to look for the unforeseen? Where does one look? If we're honest with ourselves, we must admit that one of the unintended consequences of deregulation may well be some increase in illegal activity. These consequences are especially difficult to find and tally, because they are scattered randomly across the country and, of course, deliberately concealed from the government. Sorry to say, but there is only one answer to this, and that answer is vigorous law enforcement.

We have at the Commission an enforcement staff that even the Reagan Administration's transition team has called "the envy of government." As the Commission's eyes and ears on the street, these people are indispensable. They will be all the more so as we move into an era of greater uncertainty, with novel forms of illegal conduct being arguably allowed or even prompted by our moves to ease the burdens of regulation.

These, then, are the real pillars of deregulation: a commitment to minimize the burdens of government; an active and on-going dialogue with the larger community; strong internal management; freedom of the agency to carry its ideas into practice; and the ability to make reasonable assessments of the risks and results.

Hopefully, I've made clear my approach to deregulation: I think the real key to accomplishing any task is to put in place

capable people who are committed to that job, and then to give them the tools and the freedom to do it. If you can't do that, then something is very wrong, and it will not be cured by adding another layer of procedures.

This is not to say that the regulatory process does not need some external discipline or some checks and balances. But they ought to be in the form of broad boundaries, rather than an effort to spell out in great detail the procedures every agency has to follow at every step. The key to good government is not procedure, but constant renewal through flexibility and citizen involvement.

It's an exciting time to be in government and especially at an agency like the SEC. Many things are up for re-examination. Despite the risks, we intend to move ahead. With your help, I'm confident we will succeed. Thank you.