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News Release

Remarks to the SEC/NASAA Section 19(c) Conference

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Introduction

The U.S. securities markets have been described as the "crown jewel" of our economy. During the 1980s, U.S. market capitalization increased from about $1.3 trillion to $3.0 trillion. For the decade, U.S. equities provided an aggregate rate of return of 400%. This is an excellent performance.

However, our major foreign competitors also experienced excellent growth in the past decade. In the 1990s our markets will face increasing pressure from those competitors, and the once preeminent position of our markets may be eroded.

The European Market in 1992

Europe in the 1990s and beyond will be a formidable economic force and a source of world wide competition in financial services.

As you know, in 1985, the member states of the European Community committed themselves to completing the development of a single market for goods, services, and capital by December 31, 1992. The EC has made considerable progress in turning this program into reality. The major liberalizing elements of the program either have been or will certainly be adopted.

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The post-1992 European Community will constitute a single market encompassing 325 million people, with an estimated annual Gross National Product ("GNP) of $4.6 trillion -- or nearly the size of the $5.3 trillion U.S. market.

One central theme of the EC 1992 program is that firms will have the right to trade financial services throughout the European Community on the basis of a single authorization "passport" from their home member state.

European issuers and financial service firms will benefit substantially from the reduction of regulatory barriers within the EC.

As an example of the single passport approach, the EC will permit a prospectus that has been approved in an issuer's home member state, and that complies with certain other limited conditions, to qualify for mutual recognition in all the other EC member states. It is as if -- to compare the United States and Europe -- an offering accepted in New York State, without much more, would qualify in California, and vice versa.

With respect to brokerage and investment advisory services, the EC will permit a broker or investment advisor authorized in one member country to offer its services on a cross-border basis within the EC. Or --to put in it our context -- it is as if a broker qualified in Florida would automatically be qualified in Alaska.

Under the current form of the EC directive concerning brokerage and investment advisory services, home country regulators will be responsible for monitoring firms' financial soundness and compliance with prudential rules -- such as administrative and accounting procedures, recordkeeping, and the segregation of securities. The EC also has indicated its intention to harmonize rules that regulate the relationship between investment firms and their clients.

For mutual funds, 1992 is already here. This is the result of the adoption by the Council of the European Communities of rules governing investment entities roughly equivalent to United States open-end, diversified management investment companies that invest in exchange-listed or NASDAQ securities.

These EC rules set forth minimum regulatory requirements for home country regulation. Any qualifying EC investment company complying with its home country rules may sell interests in any EC country, subject only to a host country's regulation of marketing and advertising practices within its borders. Thus, a fund qualifying in its home country will acquire a passport to sell its securities throughout the EC.

No doubt there will be bumps along the road to European unity, and the collapse of Eastern European socialism presents a huge new challenge and opportunity for the EC. Nonetheless, it is clear that the EC directives that are expected to be implemented by 1992 will permit issuers to raise capital and investment firms to offer services more efficiently than ever before throughout a huge internal market. It will permit brokers and advisors to grow as well. Further, cross-European consolidations in the securities industry may well lead to even bigger and better capitalized European competitors.

In addition to European competition, of course, we face an enormous competitive challenge from Japan.

During the 1980s, the Japanese market experienced tremendous growth. The equity capitalization of the Japanese market increased from $357 billion in 1980 to over $4.4 trillion in 1989. The "Big Four" Japanese securities firms have shown themselves to be fierce competitors in the Eurobond market, rising from relative insignificance to a leading position. Their aspirations, of course, do not end with the Eurobond market. The recent decline in the Tokyo stock market is expected to result in consolidation in the second rank of Japanese securities companies, perhaps creating huge new Japanese players on the international stage.

At the same time, the U.S. securities markets are in a period of retrenchment. Over 45,000 jobs have been lost since October, 1987. U.S. securities firms are withdrawing from a number of fields as they struggle to cut costs.

In short, in the 1990s, United States markets can be expected to confront ever more powerful international competitors from both Europe and Japan.

In 1911, when the modern era in state securities regulation began in the United States, a national financial and securities market barely existed, much less an international one. It is our challenge to ensure that United States issuers, financial institutions and markets are not at a competitive disadvantage in the 1990s resulting from a U.S. regulatory structure principally created well over a half century ago. We must permit our issuers, brokers, advisors and investment companies to compete in the unified markets that are rapidly developing in the world, for we can no longer live in isolation from world economic competition.

SEC Cooperative Efforts with NASAA and State Regulators

The Commission and state securities regulators have, in recent years, made progress in creating a unified regulatory structure. NASAA efforts in this direction are commendable. But I am deeply concerned that we are not moving quickly enough. If we fail, we may do serious injury to our economy and our country.

There are many examples of cooperation between the SEC, NASAA, and state regulators, of course. These efforts have resulted in reducing costs to participants in our capital markets. They have also led to a more efficient allocation of our limited enforcement resources.

A significant example of state and federal cooperation is our combined effort to combat penny stock fraud. State and federal regulators have benefited from these cooperative efforts in numerous areas, including training, information sharing, broker-dealer examinations, and coordinated investigations.

The Commission is pleased to have assisted in various NASAA and state sponsored securities training programs. And the states have been major participants in penny stock fraud training programs. Both the SEC and NASAA are active participants in the U.S. Department of Justice's Securities and Commodities Fraud Working Group. The opportunity for face-to-face contact between federal, state and foreign counterparts has proven invaluable in forging a stronger network of communication and cooperation among regulators and prosecutors.

Cooperation between the SEC and NASAA has also been apparent in the international arena. In 1989, the Commission proposed a multijurisdictional disclosure system for certain Canadian offerings. In 1989, NASAA's membership adopted a resolution endorsing this concept and recommending that each state implement it. Hopefully, as the Commission proceeds with this initiative, the NASAA resolution will be implemented in all the 50 states.

Another area of NASAA-SEC cooperation has been in electronic filing and data gathering and retrieval.

The EDGAR system is being developed to permit receipt and acceptance of SEC filings that also must be filed with states. It will automatically route state-related filings to the EDGAR-compatible system that NASAA plans to establish in Washington, D.C. NASAA, in turn, will transmit the filings to states participating in NASAA's EDGAR program.

State administrators also will be able to use the EDGAR electronic bulletin board feature to send acceptance or error messages to filers, and will be able to perform text queries on the public portion of the EDGAR database.

We need such one-stop filing, and we need it to be implemented quickly for all 50 states.

The broker-dealer and investment adviser registration process is another area of successful cooperation between the Commission and state regulators. Significant progress has been made simplifying the application process, once the need for registration has been determined. Over the past decade, NASAA, the Commission, and the NASD have developed uniform broker-dealer forms for registration and withdrawal, Form BD and Form BDW, and a uniform adviser registration form. These forms allow registrants to complete one document for registration in virtually all U.S jurisdictions, avoiding conflicting or repetitive submissions.

The cooperative effort that produced Form BD has saved the U.S securities industry untold costs, and made the U.S. markets more accessible to new entrants and more competitive.

However, there are many differences in state law requirements regarding who must register as a broker-dealer, and various state broker-dealer registration requirements differ in many respects from federal requirements.

These differences result in substantial complexity and costs to brokerage firms.

For example, some states limit the registration exclusion for banks to national banks and banks organized under the laws of that state. Florida limits the exclusion to banks authorized to do business in Florida, and at least two states (North and South Dakota) provide no exclusion for banks.

As another example, states generally do not require registration by agents for an issuer in an exempt limited offering. However, the application of this exclusion varies considerably. In determining its availability, some states prohibit the payment of commissions to anyone except registered persons. Other states allow these prohibitions to be waived. Still others do not condition the exclusion on the absence of commissions. All of these differences need to be addressed.

In 1983 the Commission adopted sweeping changes to mutual fund disclosure requirements to put the short N-1A prospectus in place. The states agreed to accept the new disclosure documents. Because of NASAA's efforts, state acceptance of the new disclosure format came quickly. As a result, mutual funds could use the same documents for filings with the SEC and state regulators and for sales to all investors.

In 1984 and 1985, NASAA adopted a series of resolutions to provide greater uniformity to federal and state regulation of investment companies. These resolutions, among other things, urged states to suspend or revoke fund expense limitations, to repeal requirements for filing advertising or to permit filing within ten days of use, and to adopt uniform registration and updating requirements.

Progress has been made as a result of these resolutions. In 1984, ten states imposed expense limitations. Today, only one does so. Six states have conformed their requirements for filing advertising and eight have eliminated sales reports.

Nevertheless, none of the NASAA resolutions has been completely implemented and in some areas, such as establishing uniform amendment and renewal procedures, significant progress has not yet been made.

This is a serious problem. The U.S. securities industry suffers from regulatory overload as result of the inability to clear away unnecessary obstacles to a single unified U.S. securities market, and customers suffer from inefficient and uneconomic regulatory structures.

Areas for Future Consideration

As the topics I have just mentioned show, we have undeniably made progress in creating uniform, nationwide securities regulation. Just as undeniably, more can and must be done.

The states need to review their regulations to eliminate unnecessary and burdensome requirements that may handicap our markets and investment firms. In addition, we must continue our efforts to make it simpler for U.S. firms to satisfy federal and state requirements where they vary, and take further steps to reduce or eliminate those variances.

Let me give you some further examples of where the SEC and state authorities can work together to reduce regulatory barriers, and suggest some topics for further consideration regarding the need to create a more unified United States market.

Efficient and reliable procedures for clearing and settling securities transactions are a crucial aspect of the operation of an efficient securities market. In the United States, this process is impeded by lack of coverage or inconsistencies in the commercial law of 50 states. Progress in dealing with these issues has been painfully slow. Lack of uniformity in state commercial laws governing the transfer and pledge of securities substantially reduces certainty concerning the rights of lenders, borrowers, and investors in securities. It may substantially impede the safe and efficient operation of our national clearance and settlement system.

Another area of concern is investment company regulation. The staff of the Commission has commenced a study to see, among other things, what aspects of investment company regulation in the U.S. hinder an open market in the sale of fund securities. One concern behind the study is the cost of compliance with our system of regulation, which -- of course -- includes fund regulation by the 50 individual states.

Unlike other large issuers that can rely on exemptions from state registration requirements, investment companies generally must register their securities in each state in which fund shares are sold. In most cases, the SEC's disclosure requirements satisfy those of the states. However, among other things, state requirements vary regarding when filings must be made and updated. These differences need to be eliminated.

In addition, many states do not permit funds to register an indefinite number of shares and do not provide an administrative remedy for inadvertent oversales of fund shares. Compliance with the various state filing requirements and the need to constantly track the number of shares registered and sold in each state requires funds unnecessarily to expend significant resources.

A few states impose substantive requirements on investment companies that are more restrictive than those imposed by the Investment Company Act. For example, some states prohibit certain types of portfolio investments such as options and futures. As a result, funds must either conform their investment practices to these state limitations or implement procedures so that purchase orders are not accepted from those states.

The issue of added costs and burdens imposed on United States investment companies by requiring fund shares to be registered with individual states has been raised by European officials in discussions with the SEC. State requirements in this area may present an obstacle to mutual recognition agreements with the EC countries.

The ULOE-Regulation D partnership between the Commission and the states has been ongoing for several years. Last year, NASAA endorsed several amendments to Regulation D, many of which were formulated through negotiations between the SEC, NASAA, and the American Bar Association. These tripartite negotiations are an excellent example of successful cooperation.

However, there are still states that have not adopted the ULOE. Of equal concern are variations in the requirements among the states that have adopted the ULOE, such as differences in the notification form and different "bad boy" provisions. While these differences are not significant in themselves, they impose a substantial burden on small issuers by requiring them to examine each state's particular requirements.

The competitive threat posed by the single Japanese market and the unified EC market planned for 1992 suggests that a general reevaluation of blue sky regulation is a necessary part of the process of attempting to minimize the burdens created by our federal/state system.

Conclusion

As I have indicated, the SEC has worked successfully with NASAA in the past and is committed to continuing those cooperative efforts. But cooperation between the SEC and NASAA in not enough. Major efforts are required by state legislators to address the issues of fragmentation and uncoordinated regulation. If they fail to do so we face a continued specter of a balkanized U.S. market in which U.S. securities firms will be hobbled by comparison with their foreign competitors.

Our capital markets face great challenges. We must be willing to take the actions necessary to ensure that they remain as vibrant and efficient as any in the world. Due to the vital link between the strength of our capital markets and the long-term health of our national economy, we, as regulators, must do all that we can to minimize impediments to the efficiency of those markets that result from conflicting, duplicative or unnecessary regulation.

As we examine our regulatory system in the context of a world with increasingly competitive and international securities markets, I believe it is imperative that we recognize and face up to the potential adverse effects that our dual state-federal regulatory system may have on the ability of the United States securities industry to compete internationally, and the impact that system may have on the cost of capital in this country. These are challenges which, I believe, with your help, can be met and must be met. Thank you.