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U.S. SECURITIES AND EXCHANGE COMMISSION

REMARKS BEFORE THE ASSOCIATION FOR PUBLIC CORPORATIONS

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* The views expressed herein are those of Commissioner Beese and do not necessarily represent those of the Commission, other Commissioners, or the staff.

U.S. Securities and Exchange Commission
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Good evening. It is a pleasure to join you once again here in South Florida.

When I last visited, my goal was simple: I wanted to let you know that the SEC was trying to do its share to help reduce your cost of doing business and become more competitive in an increasingly global economy.

Well, as the old saying goes, the more things change, the more they stay the same. A year later, I still want to emphasize to you that despite a new President and a new Chairman, I feel the current Commission maintains this same unwavering dedication to doing what it takes to help public companies provide what shareholders want: better performance, increased earnings and greater returns on their investment.

Of course, the hot topics of last year's discussion were proxy reform and executive compensation, particularly in terms of the Commission's efforts to tailor our proposed regulations to lower regulatory compliance costs and lessen your litigation exposure as much as possible. We realized that our attempts to improve executive pay disclosures and to bring the proxy rules in line with the current market realities would have little positive effect if these changes proved too costly to implement, or simply re-routed decisions from the board room to the court room.

But with those changes in place, the Commission now has the opportunity to address head-on the issues of burdensome regulatory costs and litigation reform. Most recently, these concerns have been highlighted in the on-going debate over stock-option accounting rules, and what seems to be a virtual explosion in shareholder strike suits over the past five years. This litigation problem is particularly acute for the innovative, growth companies that our economy is depending on for new jobs and growth. Tonight, I would like to talk more about these two topics. But with the 1994 proxy season quickly approaching, let me briefly add an epilogue to our earlier discussion about proxy reform and executive compensation.

Proxy Reform

After this past proxy season, one unmistakable conclusion is that so far, our new proxy rules appear to be working quite well. As I mentioned last year, one purpose of the rule changes was to see what could be done to foster an environment of mutually beneficial cooperation instead of mutually destructive confrontation.

I believe our new proxy rules have achieved this goal. The 1993 proxy season demonstrated that our new rules have provided a less hostile and less *costly environment for all interested parties to exchange their views and work out their differences. Amazingly, despite an overabundance of shareholders and shareholder groups seeking to challenge corporate policy, there were relatively few major proxy battles to grab headlines.*

America's ability to compete in the global economy can only be improved when investors and management can both find themselves on the same page without each side wasting valuable time, effort and money with unnecessary proxy fights. As security analysts Benjamin Gramm and David Dodd noted in their classic work Security Analysis, *removing the distrust that exists between shareholders and management may be one of the best ways to promote the flow of capital into free enterprise.*

Of course, the lack of proxy fights is no indication that management can rest on its laurels. Quite the contrary. As one street analyst who followed the events leading up to the ouster of Kodak's CEO remarked: "Either the Board gets the CEO to deliver results, or they deliver his head." Despite its bluntness, the analyst's remark is a fairly accurate description of the current state of affairs in many parts of corporate America. Increasingly, Boards and the executives they hire are finding themselves under increased scrutiny concerning corporate performance. Whether this pressure comes from inside or outside the corporation, the message is *unmistakably clear: in today's business environment, shareholders are demanding performance and accountability, and directors are heeding the call.*

Looking to the upcoming proxy season, I believe we can expect more of the same. And I encourage you, as needed, to actively engage your shareholders in discussions about their concerns. Intuitively, we all know that our markets work best when they are free from unnecessary regulation. We also know that with full and fair disclosure, markets will naturally allocate capital to its most efficient uses. U.S. corporations perform best when managers manage, directors direct and shareholders are confident that their best interests are being protected. The quality of dialogue between all participants in the capital formation process has definitely improved, which should help our markets and our companies operate more efficiently.

Executive Compensation

In a similar fashion, I believe that our executive compensation rules have also achieved their desired goal. Shareholders now have a much clearer picture of the pay that the directors they elect are providing to corporate officers.

Another positive effect of our new disclosure rules is that corporate pay is becoming more closely linked to performance. To be certain, chief executive salaries climbed over 8% in 1992, but corporate profits were also up some 22%. And if you look at the executives earning the multi-million dollar pay packages, a large portion of their pay comes from the exercise of long term stock options.

Today, stock option awards are starting to include much higher strike prices, and some are even being pegged to the amount by which the stock outperforms the S&P 500 or some other index. Moreover, stock options are now displacing other forms of compensation and becoming a larger proportion of the overall pay package.

Based on the voting patterns last year, the trend seems to be that large shareholders will not support efforts to curb executive salaries, as long as the executives only win big when shareholders win big too. This makes sense for shareholders and management alike, because their interests will be more closely aligned, to their mutual benefit. For this reason, I expect that this trend will continue. And lest you think big shareholders are not willing to practice what they preach, I note that just last week CALPERS announced that its CEO, Dale Hansen, will also have a portion of his salary linked to performance.

Stock Option Accounting

Now let me move on to the main topics of discussion: stock option accounting and shareholder litigation reform.

As many of you are no doubt aware, the Financial Accounting Standards Board has issued a proposal to require that the value of employee stock options be recorded as a corporate expense at the time the options are awarded. This proposal has been greeted with universal dismay and displeasure from the corporate community since its inception, and the debate rages on today.

Driving this debate are two opposing forces. On the one side, the accountants at the FASB and a few on Capitol Hill see stock options as just another form of compensation that must be accounted for like any other compensation provided to employees.

On the other side is just about everyone else. Some say that stock options simply can not be accurately valued for accounting purposes, and as such, they should not be recorded as an expense. Perhaps more importantly, others argue that stock options represent more than just ordinary *compensation, and that even assuming you can accurately value them, the unique advantages that stock options provide should not be sacrificed unnecessarily on the alter of technical accounting purity.*

Both sides seem to agree that shareholders might benefit from having additional information about the amount and estimated value of the stock options provided to employees, but differ on whether this information should be provided directly on the income statement, or through footnote disclosure.

Just so you know where I stand, I think we are making a big mistake if the FASB's proposals are allowed to become final. Leaving the valuation issue aside, stock options are simply too important and too valuable as tools to foster and inspire economic growth and to create new jobs for there to be disincentives for companies to use them.

Once again, as we ponder a change in the status quo of our regulatory scheme, we must weigh the ultimate costs and benefits involved. Considering that essentially the same information can be provided to shareholders by footnote disclosure, the question begged is what extra can be gained by requiring an expense to be recorded, and at what cost is this extra gain obtained.

Unfortunately, it seems that while this question is easily asked, finding who is responsible for answering it is not so easy. According to the FASB, they do not do traditional cost-benefit analysis or consider public policy issues when voting on their proposals. Their cost benefit analysis is limited only to whether the cost to gather the information and physically implement the accounting change exceeds the benefits obtained. And as far as public policy goes, the FASB readily admits that is not their job.

However, at a congressional hearing last month, the FASB also provided testimony that implied Congress should not be directly legislating accounting principles. So if the FASB does not consider public policy when writing accounting standards, and Congress, the final arbiter of all public policy, should not be writing accounting standards, at what point does public policy enter the accounting picture?

According to the FASB, the answer is never. But I think this is a misguided and unrealistic view of the world. The FASB's goal may be to build the purest accounting system possible, but the SEC's Congressional mandate is to protect investors. And in pursuing that mandate, we must recognize that there is no such thing as a free lunch, or a cost-free regulation. As you know only too well, every regulation has a cost, an impact and an economic consequence.

At some point, these costs or consequences incurred will outweigh the benefits achieved. For example, we do not have daily, weekly or even monthly corporate reporting, because the costs of that type of system are excessive compared to the marginal benefits obtained. Investors are still protected, however, because with quarterly reporting, they are able to make informed investment decisions, without the SEC forcing companies to incur massive compliance costs to provide information more frequently.

Similarly, I believe investors will be far-better off if the value of stock options is reported in a footnote rather than on the face of the income statement. By allowing footnote disclosure, we will protect shareholders' current and future investments by not raising the cost of capital for the innovative, growth companies that depend on stock options to attract and retain key employees. I've said it before and I'll say it again: the stock option accounting debate essentially boils down to one thing -- the cost of capital. And as long as we can adequately protect investors without raising the cost of capital to such a vital segment of our economy, why would we want to do it any other way?

The FASB has made the assertion that when it comes to public policy, they lack the competence to weigh various national goals. I also agree with *the sentiment that, as a general matter, Congress should not be in the business of writing accounting standards.*

But the SEC has the experience and the capability to determine exactly where to draw the regulatory lines to best serve investors and our capital markets. That is our mandate, and that is what we do, day-in and day-out.

But we may have to act sooner rather than later. As we speak, the FASB's proposals are raising the cost of venture capital. That's because venture capitalists are pricing deals based on their exit strategies, which usually include cashing out in public offerings. The FASB's proposals, however, provide incentives for companies to stay private longer -- they are able to use options more freely to attract and retain key employees, and they avoid the earnings hit that going public would entail. Even worse, as venture capital deals become less profitable because of the FASB's proposed actions, venture capitalists are starting to look overseas for alternative investment opportunities that lack the investment drag now associated with certain American ventures.

I acknowledge that the FASB deserves some degree of freedom to determine what they believe is the best accounting approach.

At the same time, however, I can not stand by idly for long and watch venture capital increase in price or even flee this country because of a myopic search for an accounting holy grail. At some point, I believe that the SEC must inject itself into this debate, and help the FASB determine what accounting approach is ultimately in the best interests of investors as a whole.

We owe it to shareholders, issuers and all market participants, and indeed our country, to make the best decision in accordance with the public good, not just technical accounting theory.

<u>*Litigation Reform*</u>

Another area where we need to decide what is best for this country is securities litigation. Or maybe I should call it the plaintiff's lawyer's dream lottery – you always have a chance to win big, and even those with losing tickets can usually settle for a prize. I am personally preoccupied with the competitive drag that litigation imposes on our society -- and I believe the SEC, Congress, state legislatures, and each of you must take up arms against the legal extortion that is increasingly driving business offshore.

I think that the SEC can, should and must play a role in the on-going debate over reforming this system. Clearly, it's broken, and if we do not fix it, it will continue to hobble our efforts to compete in the global economy.

Realistically, however, you must realize that any meaningful reform will come from Congress in the form of legislation. So far, the debate over possible reforms can be divided into two camps: first, what can be done to stem the tide of meritless strike suits; and second, what can be done to lessen the burden that securities litigation has imposed on accountants and other professional advisers.

Tonight, I'd like to focus on the former, because I believe that for most of you, eliminating frivolous shareholder litigation remains at or near the top of your wish list during this holiday season.

In my view, the most effective means to reign in shareholder litigation is to have actual plaintiffs, and not just plaintiff's lawyers, participate in the process. As it stands now, the class action system for securities litigation seems set up primarily to reward lawyers, not to compensate victims of fraudulent conduct.

As you know from your rising insurance rates, most securities class actions settle. Recent studies, however, suggest that settlement values do not necessarily reflect the merits of the cases. Indeed, if strong cases are under-compensated and weak cases are over-compensated, the Commission's reliance on private actions to compensate victims and deter fraud may be misplaced.

Moreover, the systemic costs involved in utilizing securities class actions to compensate victims appears highly inefficient, and imposes significant costs on all issuers. In some cases, the lawyer's fees equal or exceed the plaintiffs' recovery. In other cases the transaction costs nearly equal the net amount paid to investors. For example, if a case settles for $7 million, the plaintiffs' lawyers may get $2 million, and the plaintiffs $5 million. But if the company also has to pay another $2 million for its own legal fees and other expenses, the bottom line is that the issuer pays $4 million to re-pay investors a total of $5 million.

Of course, while I say that the issuer pays $4 million, you and I know that insurance companies are also footing part of the bill, and that means rates go up for all. At best, class action settlements simply transfer money from one group of shareholders to another. At worst, through higher *insurance rates, class actions cost all shareholders money, even those at companies that have never been sued, if such companies still exist.*

Clearly, if the goal of the system is to compensate victims as efficiently as possible, and to protect investors as a whole, the system has a long way to go.

One possible solution is to introduce measures to prevent plaintiffs firms from using professional plaintiffs or otherwise maintaining an inventory of shareholders to serve as nominal plaintiffs. I'm all for compensating the victims of fraud, but let's make sure we have real victims and not just hungry lawyers before the litigation papers start flying.

But this is just the start. To have a greater impact, I would also like to see special masters or a committee of plaintiffs utilized to more closely align the interests of class counsel with those of shareholders. This would be particularly helpful for those firms that operate litigation factories, where the pressures created by lost opportunity costs may give these firms an economic incentive to bring and settle five marginal cases quickly, rather than litigate one meritorious claim to a successful conclusion.

Finally, I would like to see some sort of fee-shifting provision applied to fraud claims where the case is found to have no merit. By amending Section 10(b) to include a fee-shifting provision, we could deter frivolous claims without a significant chilling effect on meritorious ones. And by using legislation to put this mechanism in place, courts may be inclined to use it more frequently than they currently use Rule 11. I must warn you, however, that as appealing as this solution might appear, attempts to introduce even a modified version of the so-called English rule may run into rough waters on Capitol Hill.

These proposals represent just a few of the suggestions being actively discussed at the SEC and in Congress to curb the problems caused by frivolous shareholder litigation. Legislation is expected to be introduced early in the next session of Congress, so the debate is likely to become quite a bit more active soon. It is my hope that this renewed activity will finally produce some form of relief in an area that desperately needs it.

As the debates over stock option accounting and litigation reform continue to rage, I welcome your suggestions and input.

At the end of the day, however, whether the SEC must decide to take a more active role in the stock option debate, or ask Congress to reform our *system of securities litigation, one central issue will weigh heavily on my mind: in our continuing efforts to protect investors, has the SEC done all it can to help reduce your cost of doing business, and help your companies become more competitive in an increasingly global economy.*

Unless the answer to that question is a resounding yes, you can rest assured that I will do all I can to keep fighting to see what more can be done.