Securities and Exchange Commission Historical Society
Interview with James Doty
Conducted on March 10, 2010, by Kenneth Durr

KD: Interview with James Doty, March 10, 2010, in Washington, D.C. by Kenneth Durr. You mentioned that you were from Texas. When you went to Rice, did you anticipate on being a lawyer?

JD: No. I thought I was going to be a historian. My graduate work, until I got to law school, was in European history and some focus on British history. It was, I think, the work in British history that made me think of being a lawyer. Many of the most interesting figures in the 19^{th} Century just happened to have been lawyers. Lord John Russell, pretty important figure. Then the United States had its own group of people who were legally trained, if they never practiced. I believe it was in the course of being a graduate student and looking at what you did in history that made me think that I would be happier as a lawyer, and that I should not expect to be as successful or as good a historian as many of the people around me. I thought that, probably, I'd be a better lawyer.

KD: You were in the graduate program at Rice?

JD: No. I went from Rice to Oxford. I was two years at Merton College, Oxford. I came back, I entered the graduate program in history at Harvard, was ABD. I took my orals with David Owen as my instructor, my studies director, and with David Landes. Landes was, at that time, getting into the kind of economic history that he has done since then, which has been so important, and which led to *The Wealth and Poverty of Nations* as his cornerstone book on why economies succeed.

That didn't push me away from law. On the contrary, it pushed me in the direction. Much of the work being done at that time was either focused on econometric or quantitative content analysis. At Oxford I had dipped into revolutionary movements in France. Charles Tilly was doing a lot of that work, a young professor at Harvard. I did some graduate work for him, and in the kind of work David was doing, and it led me to look at the Encumbered Estates Act in Ireland, and to study how British economic and legal theories had been the background of very forceful and intrusive economic policies, which were then applied, experimentally, to Ireland.

They tried a kind of financial services reform that involved wiping out the prior encumbrances on land in hopes that it would bring economic value out of the land. It did not. But the whole of it has a certain resemblance to things that we've seen since then. It is the intersection of public policy and economics with a heavy emphasis on land. That convinced me and made me think that lawyers needed to come to grips with some of these problems. It also had its effect on what I did in law school. I left the Harvard graduate school after I had taken my oral exams, and I had a real decision then because it was either go into the dissertation mode and look at at least one year and probably two, if you were going to do it properly. The reward, the payoff for being a successful candidate would be to have the two years to do a good dissertation and publish it. That was going to preclude, I thought, going to law school.

Instead, I went over to the Yale Law School. A wonderful man, Jack Tate, who was the Dean of Admissions, decided that, notwithstanding my rather abysmal performance on the Law School Aptitude Test, that I might turn out to be a decent lawyer. I got into Yale Law School and thought that, given what I had been reading in British history and European history, I probably ought to learn what the capital markets were based on as legal theory.

I didn't really head toward litigation or clerkships. We were very immature at that age. I had thought that I was going to take the background I had in social and economic history and constitutional history and translate that into some kind of theories about market regulation and securities law. I didn't know the terms market regulation then. I had just decided that corporate law, generally, the shape of the economy was something I should be looking at.

I came out in 1969. I had been close all these years to a very brilliant guy, a man named Ewell E. Murphy, Pat Murphy, who was a partner in international law at Baker, Botts. He became, subsequently, the director of the Fulbright Foundation. He had had a very strong influence on my career choices. I went to Baker, Botts largely because of him. It was not unrelated that Rice's counsel was Baker, Botts. In other words, there was a mystique about the firm based on its historic relationship to the university.[1]

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[1] There were other important role models there for a young lawyer: among them, Frank Wozencraft who had served in the OLC with Nick Katzenbach.

KD: Tell me about developing the practice there. It's clear that you had this abiding interest in economics, which was leading you.

JD: Untrained as an economist. Just looking at it as a historian which, as you know, is not the same thing.

KD: Right, exactly. But that may have been a benefit if you're looking at it as a lawyer. Did you find that?

JD: Yes. It made me want to get into government and public policy, and it made me want, as a young lawyer at Baker, Botts, not to simply be a success in the traditional terms of a corporate lawyer in Houston, at that time. My timing was impeccable. I hit the legal market at the time that the equity markets went into a decline. It was a protracted decline. I found myself doing very many different kinds of work. We had a case, a merger and acquisition proxy fraud case that I became helpful to the partners on, and it went all the way to the Supreme Court. It still stands as an interpretation of soliciting materials in the context of a merger. It has the uninspiring caption of *Smallwood v. Pearl Brewing Company*.

There was a lot of financing work to be done. I went, eventually, to Indonesia and to the Orient for Huffington, working as a young lawyer on what we would now call project development. Before the public distribution of the securities, it was just a secured financing based on the cash flow of the LNG development in the Pertamina fields of

Bontang, Indonesia. Roy Huffington had been something of an Indiana Jones. He'd gone out there and found this gas field and established the confidence of the Indonesian Government. We were financing trains of LNG development with Pertamina and with the Industrial Bank of Japan.

I came back. We had brought into this office a very fine lawyer, Jim Treadway, who had been a very influential commissioner with John Shad. I was standing in the conference room at White & Case in New York closing the last train of the Pertamina financing that I did when Treadway called me and said he was leaving the firm to go to Paine Webber, where he became general counsel.

On the plane home, I began to reflect on the fact that Treadway had been brought into this office to begin a kind of SEC regulatory practice. He had hired some young lawyers who were very good, one of whom is now in the Houston office, David Powers; one of whom is now a successful manager of money here, Stephen Quamme.

KD: Had you worked with them?

JD: Yes, I had known them. One of them was James A. Baker, IV, Jamie Baker, who has just come back from Riyadh, and who is now the partner in charge of this office. You had these young guys here who were planning on doing corporate and regulatory law. So going home on a plane, it occurred to me that the Washington office was now without anyone to direct their work, mentor them, be part of what was the plan. That night, I explained to my wife, who was the mother of two very small children at that time, that I wanted to think about moving to Washington to do this. She did not threaten to divorce me. She looked at me as if that was a rather odd idea, but one thing led to another. That was in the spring, and by the following summer, we were here. That was 1987.

KD: Okay.

JD: I came to Washington in ‘87. One of the young lawyers that Jim Treadway had brought to Baker, Botts was a bright young man named Richard C. Breeden, who had been a lawyer for George H.W. Bush. He had helped George H.W. Bush with something called the Task Force for Financial Reform. He had written a large report. The partner heading the office then was Perry O. Barber, who had worked for Jack Valenti in the Johnson White House. Of Breeden, Perry said, “This is someone who’s going to be valuable and around Washington for a long time.” Perry brought me into this office, and Richard and I became close friends here. In 1988, he went to the campaign. In 1989, January, he went to the White House. In August-September of 1989, he became the youngest chairman of the SEC since William O. Douglas. He was thirty-nine years old. He was kind enough, to include me – when he started doing confirmation prep, I went over with him and saw how confirmation prep was done.

KD: How was it done?

JD: The White House assigned a very astute, skillful guy, whose name I'm afraid I've forgotten, but George H.W. Bush's administration had him come in and arrange meetings between Richard and senior staff members at the Commission to brief him on what the Commission agenda was, what was happening. I will never forget, he sat down with Richard. He said, "The first thing you do in your confirmation hearing, you say you want to thank the President of the United States." He said, "I can't tell you how many confirmation hearings I've seen where a presidential appointee comes in and forgets to thank the president for appointing him."

His advice was that very kind of solid, practical advice. He took Richard around the Hill. He introduced Richard to people like Don Riegle. We had what the country most wants and needs, and what we most now want. We had a Republican White House and a Democratic-controlled congress. People had to work together. A lot of the stuff that we're now regretting could've happened, but didn't happen and the results were historic. The shape of securities regulation changed in some ways that we'll talk about in this interview. Richard began by meeting with people in a Democratic-controlled congress.

Riegle was chairman of the Senate Banking Committee. I think Phil Gramm may have been the ranking Republican by then, but I'm not sure. John Dingell chaired the very important Energy & Commerce Committee in the House. Ed Markey was the subcommittee chairman for securities. Bob Michel was the ranking Republican. Many of these people are no longer on the scene, of course, but it was a very skillful group of legislators who were in place at that time.

KD: You were talking with Breeden as he's going through this?

JD: Richard would have me over to see the confirmation process, and that's how I began to meet some of the people who were senior staff. The next thing that happened, though, was after he was confirmed—he was confirmed without incident. I think in the course of confirmation, because of his work for George H.W. Bush on financial services reform, he had established a lot of credibility on the Hill. If you go back and look at the Blueprint for Reform, as it's called, you will find many of the ideas both fresh and astoundingly mundane because many of the things that we now are taking as being so obvious had been discussed in great detail.

The need for derivatives regulation. The need to unite the equity markets and the derivative market regulation. The risks of the banking system, which was evolving major bank holding companies, but had nothing in place to deal effectively with the "moral hazard" of insured deposits, subject only to the prudential regulation of the FDIC. The commitment of the Fed to banking expansion to meet foreign competition, made them willing, along with the Office of Comptroller of Currency to overlook the erosion of Glass-Steagall boundaries de facto, and the inability of the SEC to really do much more than regulate some of the isolated securities activities of major bank holding companies. All of this was clearly seen, and it was discussed.

The next thing that happened was that I went off to New York again for some corporate purpose. By then, I was living up here. We're now talking about the fall of 1989. I went off to New York. I came back one evening. I'd been working all day, I had not had any time off, and Richard had said, "Come by the Commission and see us when you have time. Come see how we're doing." And so I got off of either the Amtrak or the air shuttle and I went over to the Commission at 450 5th Street. They cleared me up, and I went into his office, and it was clear that all hell was breaking loose. It was the October, 1989 market break.

I got there about four or five in the afternoon thinking that I would pass a little time with him and chat. I didn't leave until I think about 1:30 or 2 in the morning because it was a wonderful scene. They were on the line with the Secretary of the Treasury, the Federal Reserve Chairman and with various European banking heads. Rick Ketchum, who was then the head of the Division of Market Regulation, Rick (along with Bob Colby) was staying in very close touch with all of the firms, the banks, the securities firms. How much capital did they have, how much did they need, what were their overnight commitments, what was going to happen to their liquidity?

Linda Quinn was also polling major registrants. The Commission, of course, does not regulate, has no real periscope insight into, the liquidity of non-financial service firms. They have a duty to disclose their liquidity and capital requirements. Linda (along with Elisse Walters, Meredith Cross) was checking around to determine what was going to happen to them, what they thought might occur, and she was also talking to people like

Jim Robinson, I think, at American Express and others who were on the margins at that time of financial services. A lot of work was being done to suck in information to find out what was going to happen when the markets opened the next morning. (I think this was a weekday. That is, I think the markets still had a day. I can't remember this, but I do not think a weekend interceded. I think the question was whether the markets are going to open again.) They were being asked, "Are the markets going to open?" And they were saying yes. [Laughter]. Generally, they were sending the message out that, yes, the markets are going to open. It was a case in which there was a lot of quick response. It was shortly after that that Richard suggested that I come over there and take a job, and I did.

KD: Now you, initially, came in as an assistant or something like that. Is that right?

JD: I came in as Counselor to the Chairman.

KD: Was that a new job?

JD: It was a new job, I believe. Mike Halloran, subsequently, did this. When Mike Halloran went to the Commission, he went in as Counselor to the Chairman, so it's been used since then. (By the way, you should talk to Mike Halloran about how the events we're talking about fit with and blend into the events that Mike saw.) On the whole, it was a wonderful demonstration of how the Commission could operate in crisis. The building was small.

It was run down. People were cramped. There was a tremendous sense of *esprit de corps*.

I was there by April of 1990. I had to wrap up things here. Between October or November—I can't remember when Richard actually made an offer—but it was somewhere between October-November and January-February that I was able to start getting things in order.

KD: Now when he brought you in as counselor, and this is still fairly early in Richard Breeden's term.

JD: Comparatively.

KD: Did you have discussions about where it is he wanted to take the SEC, what his agenda was like?

JD: No. He said he needed a consigliore. He said he had a lot to do, couldn't do it by himself, and that they were going to have major legislation coming up. I think he already had in mind some of the legislation that we're going to talk about in a moment. I remembered going over and sitting down with senior staff after this decision had been made, and some of them I had not met; others I had, such as Linda and Richard, Dan Goelzer, Linda Fienberg, who is now at FINRA. There were some of them I hadn't met, but I sat down with them, and it was clear to me that Richard was very much a hands-on interactor with the senior staff, and that was important.

That was important to me in terms of what I was going to learn and do, and it was important to, I think, the Staff. It became increasingly important. Richard had tireless work habits. He would often convene staff at five and six in the evening, and we would be there until eight and nine, sorting out, discussing what had happened during the day. This was after the market break and after so-called speed bumps, but after that, on any number of issues that we'll get to.

The great advantage of being at the Commission in this period was that it was a committee of the whole senior staff that met with Richard and met with commissioners. Among the commissioners were Richard Roberts, who was an expert on PUHCA, and who began, I think, to get the Commission thinking seriously about the fact that it should change its view of holding company regulation. They had always opposed it, but the reason why they had opposed it had not been convincing to Congress. They had opposed it on the grounds that it was a distraction from the real business they had. And it was merit regulation that didn't fit real well with what was, on whole, a disclosure regime.

Richard Roberts, Richard Breeden and others in the Commission, I think Mary Anne Smythe, who was the investment management head, that had jurisdiction of that, began to rethink how to frame the regulatory system under PUHCA in a way that showed Congress it was really obsolete, and that it was deterring progress. Consolidation and convergence became the buzz words. We can get to that. On the whole, it has not worked out so badly, notwithstanding the California energy crisis and a lot of that. On the whole, I don't think anybody wants to go back to SEC regulation of holding company finances and transactions. That's been a fairly smooth transition of some authority to FERC, and a lot of authority to state regulators.[2]

Anyway, that was going on. A young commissioner named Mary Schapiro had just been re-nominated by Ronald Reagan to the Commission. Mary had already served at the CFTC with great distinction. She, of course, went back subsequently to the CFTC as Chairman. But, in fact, she'd been a Commissioner at the CFTC, and she brought a lot of insight into what was going to happen and what did happen when a lot of these issues became front and center.

Phil Lochner was brought on. Phil is an extraordinarily gifted lawyer out of Cravath. He had known Richard in his early days. Ed Fleischman became a very important Commissioner in some very important ways. There were huge arguments between Richard and Ed Fleischman, some of which erupted in the public, but the important thing was that Ed had an enormous positive effect on everyone's thinking, including Richard's. And Ed was formative about a lot of things that went on at the Commission in very important ways. So it was a good Commission, an active Commission.[3]

[2] For a brief time Joe Grundfest enhanced the Breeden Commission. I think he and Richard Breeden were in many respects kindred spirits. He soon left to return to academe.
[3] It is important to recognize and remember Carter Beese, who brought to the Commission a venture-capitalist's view and experience.

KD: There was a lot to do. The legislation that you mentioned is really the first big thing on my list, and I want to talk about that. You had two big landmark things that came through in 1990. You've said a good bit about what was driving this, but I wonder if you could sort of give me a little more, the SEC's understanding of what Congress wanted, what was necessary, and what your process was. I know as general counsel, you were probably involved in some way in helping frame the legislation.

JD: We had two very gifted legislative affairs directors, Mitchell Delk, who was succeeded by Katherine Fulton. And they were very good at working with Martha Cochran, who was then Senator Dodd's and the banking committee's principal legal advisor, and (on the House side) Consuela Washington and Steve Blumenthal. A lot of work, a lot of give and take and education between the SEC senior staff and the Hill took place exactly in terms of what was needed to address the S&L crisis, what we're learning from the S&L crisis, what had been the problem and what should be done about it. New legislation, FIRREA, had just been passed, Financial Institutions Regulatory Reform and Enforcement Act. (People joked about the fact that initially it was thought that it should refer to "depository institutions," which would've made it read DIARREA, so they didn't do that. They went to FIRREA instead. A lot of jokes about that at the time.)

FIRREA had been a very important piece of legislation that had made securities lawyers and banking lawyers talk to each other in a way they had not before because of the remedial features. There was grave concern on the part of many practitioners of my age now and my background, who included Ed Fleishman and lawyers around town like

Dennis Lehr and others, who thought that it was dangerous to give the SEC cease-and-desist powers. There was discussion about whether or not Congress had gone overboard in vesting the SEC with augmented enforcement powers.

KD: This is the enforcement remedies?

JD: Yes.

KD: There were several things happening at once.

JD: Exactly. You have to put the S&L crisis in the context of Ivan Boesky and the largest insider trading scandal that we had ever seen on Wall Street since probably 1930s. This had been something that had come to a peak under Reagan and the Ruder administration of the SEC, but it had a long tail. So when Richard came in, Michael Milken and Dennis Levine and Ivan Boesky were, all of them, still on the agenda of the Commission. The insider trading, the leaking and the malfeasance in the banking industry that led to some people going to jail and being frog-walked out by Rudy Giuliani, all of that was very much in people's minds.

Along with that, you had in the S&L crisis a clear example in the minds of many people of what happens when you can play with the house's money and when people ignore risks, the risks of legal sanction and think that they have unlimited access to the Fed window, when they don't. You also had a major scandal involving an attempt by Salomon Brothers to corner the auction, the Treasury auction.

KD: That came along a little bit later.

JD: 1991, I think. You can look it up, but I think it's 1991. This is all precipitated by a guy named John Meriwether, who doesn't really have his career ended by this, and who crops up again in a company called Long Term Capital Management. And you can read about that in the book *When Genius Failed*. You are seeing in the Long Term Capital Management and the S&L crisis patterns of conduct that are replicated in Bear Sterns, and Merrill Lynch and Lehman Brothers. There are details, changes in the way in which the failure occurs, but some of the same people are involved, and the same misapplication of risk. Because we can all make an investment that we know is completely risky and that there's no assurance of return if it's a trivial amount of our expendable cash. These were investments in which it's believed there was absolutely no risk that they would not come out right, so the amounts of capital were extraordinary. They were imprudent on their face. And the risk was the firm's capital.

KD: Tell me a little bit about the general counsel's office, how things were set up as you came in, and how you worked with folks on the legislative front.

JD: There's a front office and a back office. The front office of the general counsel's office is the general counsel and the solicitor, Paul Gonson, the associate for appellate, Jacob

Stillman, Phil Parker, who was the associate for legislative policy. There is an associate for litigation – Richard Humes, first African-American to hold the post – appointed by Richard Breeden. Then there are assistant general counsels and others. Diane Sanger was an associate general counsel, became an associate general counsel, I think, for legislative policy or regulatory policy. It was very much a consultation body that had to fight to keep its hand in enforcement issues, and its hand in legislative policy or rulemaking.

There had been substantial addition of counseling, legal counseling, in every operating division, which had been, really, a good-faith effort to provide promotion for long-term members of the staff. But as a result, you had little mini-general counsel's offices in every operating division.

Two things made that work well. One was that Richard, I think, for me and as a great help to me, whether consciously and deliberately or not, projected the assumption that when there was a meeting on rule-making enforcement or market regulation or legislation (something big), he didn't want to go in a meeting and find out I had not heard about it. In other words, it had gone around the building that the General Counsel was somebody that you needed to bring initiatives to before they became mature for presentation to the Chairman. It didn't always happen, but on the whole, it happened. The second thing is that we had an extraordinary senior staff.

All of these people who were the senior staff, became good colleagues and friends because of the kind of operating ritual that I described before. We were all going to be sucked into the Chairman's office at different times during the day and find ourselves having to plan with him, or think out loud with him about what to do. It became apparent that you could be their advocate and build trust and confidence as you do. The General Counsel is the lawyer for the whole Commission. There were times when Commissioners expected the General Counsel to put out extra effort for them. One of whom was Mary Schapiro, when she reformed the Rules of Practice; one of whom was Richard Rogers, when he was concerned about cases under 102(e) that involved accountants or Public Utility Holding Company Act initiatives.

You could do that, and you could preserve your relationship with Richard Breeden as the Chairman, at the same time building trust and confidence with other Commissioners and with the senior staff. It's not a very complicated formula, and it's one that Arthur Levitt articulated publicly at one time and, in fact, worked for Arthur. He had good general counsels, and they worked with him well, and the result was good. I think it's one that can be found in the successful roles of any general counsel. I think it works out that way. You become someone who is a legal advisor to more than just the chairman. It helped that staff between the chairman and the operating staff, the division heads and office heads was thin, it was not heavy.

It was a source of frustration for all of us that it was hard to get our work with the back office with the whole office done, and spend the time with each other and the Chairman that we had to spend and on the Hill. So? That's the job. That's why you're there as senior staff. I think that is what emerged as the ethos of the Breeden Commission, it's why Richard was missed, it's why he accomplished so much. And he accomplished the Penny Stock Reform Act, the Remedies Act. He got the repeal of PUHCA going. He accomplished reformation of investment company regulation, which came out of the special study that was done. He accomplished the reform of the government securities auction market. He accomplished the establishment of procedures and processes for settling lawsuits that hadn't been tried before. He made greater use of ancillary relief. Some use had been made. It wasn't that he invented it, but he made enormous use of ancillary relief. He kept the Commission in the game on market structure and CFTC reform. He involved other Commissioners in this as well – Mary and Richard Roberts made big contributions to these initiatives, some of which continued into the Levitt Commission.

When I returned to this office again, the Chicago Merc was giving up space in the building. We took the space. I salvaged these posters you see on my wall because they are the essence of what the Chicago Merc's message was at that time, and it was that no regulation by SEC should be extended to the futures market. Mary warned Richard: Mary said, "We have got to realize how strong that blowback is going to be." We had, as the Chairman of the CFTC, we had the spouse of the ranking Senate Republican: Wendy Gramm was the CFTC Chairman. It was not easy for Richard to keep his position on market structure and the importance of having a single regulator that regulated the equity and the derivatives markets, and that had a simple mission of transparency in investor protection, as opposed to the moral hazard of the Fed and its bank supervisory role, which was to cultivate the greater financial capacity and business activities of banks. Not an easy thing to maintain a balance.

KD: And some have said that maybe Breeden spent a little too much capital on that particular fight.

JD: Why? He got what he wanted. What do you think he didn't get?[4] Oh, by the way, 144(A), 145, the rules which have created immediate access for business to the capital markets and have really reduced the friction whereby capital raising occurs and which have come to eventual fruition in the last round of public offering reform: All of that was done by Linda with Richard Breeden's support and encouragement. She knew exactly where she was going. Cross-border offering reform, all of that was in Linda's mind.

KD: 144(A), was that in the works when you came in?

JD: Yes. She was well along with her thinking. Lee Spencer, a classmate of mine from Yale, a wonderful guy who had been director of Corporation Finance, he had been there along with John Huber and Linda, they all began the integrated disclosure regime. By the time I came, the integrated disclosure regime was in place. Linda knew that you had to carry it forward into some practical areas. There had been a concept release on globalization, which was Linda's. She worked that through with some very talented members of the

[4] I do not suggest he got merger of the SEC and CFTC, of course. He got the Remedies Act, and the reconsideration to GAAP accounting, discussed below; and he is clearly seen now to have been on the right side of the derivatives issue.

staff who are now out in practice. I'm going to get to where I think this ends up, and it ends up with investor protection on the accounting side, maintenance of GAAP was the moat, that was the firewall that Richard stood firm on, and he won.

They liberalized a lot of offering mechanics. They invited in foreign offerings, but they insisted that the numbers had to be right, and they had to be reconciled to GAAP. This was very contentious. There are some interesting stories about that. But he did all of that with Linda's help. He not only let her do it, he encouraged her, and he was a source of inspiration and support for her, and she was a source of real wisdom and advice to him and to all of us. He reformed the modern public offering structure. He began it all, and the rest of it just falls into place. Not without cost. Arthur Levitt had to fight hard for it. Others had to fight hard to get where we are today. But it wouldn't have happened if you hadn't begun with 144(A), 145, the cross-border offering rules. Meredith Cross, I think, will confirm some of this.

KD: You talked about this being contentious, however. Was there contention within the Commission itself?

JD: I think that Ed Fleischman was someone who was always thinking about how enforcement was going to affect market activity. We had a contentious case that was hanging on, and that was the Kern case. But guess what? As a result of Ed's creativity and Richard's creativity, it got solved [laughter]. That is to say the Kern case was resolved, gotten off the Commission's agenda, became no longer a source of contention, and the remedies that it got passed were the cease and desist order that allowed prospective general relief. It's very hard for me to see where Richard sacrificed significant political capital. He knew how to work the Hill, he knew more about working on the Hill. He had the confidence of people on both sides of the aisle, and he got it done. His audacity was in some respects his formula for success.

The one thing he did not get done is something that is still not done. He did not get one integrated regulator for the equity and the derivatives markets. Wow, you know [laughter]. Gee whiz. (There must be something *really hard* about that!)

KD: But in some respects, at least as far as financial futures, that's what he was trying to get.

JD: He saw, clearly, the need to do it. He saw the fact that so much of the market's activity was shifting into this area that you couldn't monitor and determine capital requirements. You need to talk to Mike Halloran, especially, about this. But capital requirements, which now loom so large, were recognized as being a moving target and a problem. First, Michael Mann and Michael Macchiaroli (the latter is still at the Commission), were constantly working in Europe to avoid having European regulators and bank regulators use capital requirements in the name of prudential regulation as an anti-competitive tool, to keep U.S. financial services firms out, to require that they capitalize the in-country operations at a rate that would make it not profitable. That was going on.

At the same time, over here, Richard was trying to work into the consciousness the fact that margins were too low on derivatives. Shocking idea, that margins would be too low on derivatives! But everybody in the securities industry knew the margins were, and had been, too low on derivatives. Richard announced the very contentious position that, gee, you know, you should raise margins at times when you're not under financial stress so that you can lower them when you are under financial stress. He was trying to get margins on derivatives up and to create more effective regulations of margins. He was being opposed by a lot of people who didn't want to do that. They had good business reasons for not doing it.

KD: There were some folks behind this too, like Alan Greenspan and some fairly influential people that thought that the SEC should get this additional –

JD: Well, if you read *The Age of Turbulence*, which I have in my bookshelf down here, it is my impression that Alan Greenspan as the Fed Chairman, he could speak for himself on this, but he has never been in favor of derivatives regulation. He didn't want derivatives regulation. When Brooksley Born was head of the CFTC and wanted to regulate the derivatives on currency, he and Rubin and Arthur got in a meeting and told her she shouldn't do it. Arthur, to his great credit—Arthur Levitt was a great successor to Breeden, has been a great chairman—and Arthur, to his credit, has said we were wrong. But I think it leaves the beach ball pretty much where it belongs.

I think Robert Rubin did not want, as Secretary of the Treasury, to have a fight on his hands with powers in Chicago, and I think Greenspan, actually, was philosophically committed to the idea that it was a bad idea. Certainly, Phil was. Phil Gramm had editorials in the *Journal* at that time about how the SEC was coveting—wanted to regulate this little industry that it had long held in contempt because now the industry was big and profitable. I think most of the powerful opinion makers at that time were against trying to unify the two. If there's a historical record to be corrected here, I'm open to it.

KD: I think that's true in general. There must've been some support, though, for him to carry it as far as he did.

JD: No. I mean, maybe I don't know. Maybe there's something that I'm not aware of, but I think, first, the established equity markets, the New York Stock Exchange, the American Stock Exchange and the NASDAQ probably would've liked to have seen it. I do not believe that they can be said to have gotten out in front of this. After all, the Fed Chairman had something to say about their business as well.

KD: Something else that you talked a great deal about, at least early on, '90 or early '91, were shareholder issues. Was that part of this package of reform that Breeden was looking at? Tell me a little bit about the discussions there and what the general counsel's office's role was in that.

JD: Richard believed, even then I think, that it was wrong for management to be self-perpetuating. People were tinkering with and considering proposals that looked like direct access, what we're now looking at. Certainly, the Commission, I think, established a position of encouraging shareholder proposals under Rule 14a-8: it was Linda's clear position, and I think it was certainly backed up to the hilt by Richard and other members of the Commission, that anything having to do with control, with continuity entrenchment of management was strategic, was not ordinary business. They were going to let those proposals in. They were interested in going beyond the Catholic Relief organizations and organizations of religious persons who were concerned about child labor, or concerned about the treatment of women and children in countries.

The Sullivan Principles had a very heavy influence on this. The Commission was encouraging of resolutions on doing business in South Africa. I think there was a perception that that had had an effect on the way American corporate life viewed investment in South Africa. Likened to it was tobacco, the investment in tobacco. You can see in some of the proposals which Meredith Cross's Division of Corporation Finance has published within the last weeks,[5] you can see resonance of the Commission's staff decision that, somehow, investment in tobacco has a business orientation that is strategic, and that shareholders should have disclosure about it. They should know whether management is thinking about it. They should know how management is evaluating its investments in South Africa and tobacco. And now climate change.

[5] I refer here to The Climate Change Guidance, which acknowledges the influence of these earlier initiatives, including the Y2K Interpretive Release.

This came up again with Arthur Levitt in Y2K: what are they doing out there about data processing? We're going to see data security, cyber security. I would just say that these are small waves that began in the middle of the Pacific. They were not as controversial, but they have built, and they have been significant waves now. You can't get to where we are now with climate change and some of these other issues without seeing their origins.

They did other things, the Commission. It was a very significant time for enforcement. Among the enforcement targets, Milken was powerful in that he could afford to litigate, and he was well-represented.

Arthur Liman provided brilliant representation to Michael Milken. There was public pressure: People wanted to see the Commission take all of Michael Milken's money and strip him of his wealth. People had to be reminded that we had to prove violations of the law to do that. So the Commission stood by its guns on that. At the same time, it went after others in a big way who had, perhaps, proceeded with a certain buccaneer, cavalier view of all of this.

Lawyers begin to be important: Richard's famous statement about O'Hagan, that he wanted to see O'Hagan left naked, homeless and without wheels. Why was that? Because O'Hagan was a lawyer, he was an inside guy. The role of lawyers in implementing and contributing to violative conduct is very important. There's a balance to be maintained. Ed Fleischman is very concerned about it, speaks publicly about it. It's not an easy question.

Before that, the last great scandal had been the National Student Marketing scandal where you had a merger involved. A lawyer delivers his closing opinion that says the conditions of the merger have been satisfied, when he knows that one has not, there has not been a delivery of a comfort letter. We had thought for a long time, in 1987, 1990, we in the bar had been thinking for a long time the way you really get in trouble is by delivering your opinion, by relying on certificates that you know are not true. Those are still problems, of course, but what you see in the contentious cases the Commission is dealing within the '90s is lawyers who are helping make decisions on disclosure, who are in the middle of strategic planning for tender offers or mergers. O'Hagan was trading on non-public information, but the theory of misappropriation had not been established.[6]

In addition to the remedies act, and it's the remedy of cease and desist, in addition to the remedy of imposing fines and penalties on regulated firms administratively, you had also new theories of enforcement that are with us now. He was a strong law enforcement chairman, and he backed his enforcement division.

KD: I saw a mention of a 102(e) group that appeared to have been in the general counsel's office.

[6] We address the controversial 21(a) report on the "noisy withdrawal" issue later in this interview.

JD: Yes, we had it there. Going back to the time of Edward Green, it had been very important that the general counsel made the decision on whether to bring a 102(e) case to the Commission and get authority to proceed, and they handle the case.

KD: Why was it important that the general counsel do that?

JD: Because it was felt, I think properly, that as lawyers, they would be able better to make the decision of whether the conduct of the lawyer transcended merely counseling and giving advice. This is the issue which Bank of America is going to raise, by the way. This is what is at the center of what Judge Rakoff was trying to get at and didn't get at in Bank of America. If the lawyers give impeccable legal advice and tell people, "Here's the up and here's the down, here's what can happen, this is your decision," to what extent is that merely counseling?

By the way, there was a strong proposal at that time which surfaced again for a lawyer snitch rule. There has been constant questioning of the role and duty of lawyers who sit in that meeting and who listen to the deliberations and who hear that, in fact, the CEO or the CFO says, "I don't care whether there's a risk here, I don't care what the lawyers say about this. This is survival and we're going to do it." This came to a head in the Salomon Brothers-Gutfreund case, it comes again in the cases that arise from time to time on the Breeden Commission, but they're not very hard cases. The hard case is Bank of America. We don't know what the facts are.

The question will be at what point is it good policy or bad policy to put on the legal profession the duty which accountants have under Exchange Act section 10A. I don't want to predict that, but I think the view has always been, or was within the Commission, before you proceeded against a lawyer, you wanted to have the general counsel and the general counsel's office decide whether there really had been a breach of professional ethics.

To explain the point at issue for lawyers, the question was: "Had they done something which, <u>as a lawyer</u>, was unprofessional?" That was a predicate of 102(e): 102(e) was a disciplinary rule, so it was thought to be something that, when professional conduct was involved (accountants, engineers or lawyers, by the way), you wanted to have the General Counsel take a hard look at that, initiate it and litigate it. It's been moved to the Division of Enforcement. The world hasn't changed dramatically. I think the issue hinges more, the protections and the balance hinges more on the personnel of the Commission, the balance on the Commission, the judgment that the Chairman and her Commission have, and the way in which they listen to and evaluate cases that are proposed. That's where the discipline occurs.

KD: Was there some attempt with this group to come up with criteria by which to evaluate or some way to systematize this rather than just have it be a matter of judgment each individual time it comes along?

JD: There were pinpricks of cases. I left the Commission at the end of 1992, end of December of '92. There is a case, *In Re Feldman*, in which a lawyer is telling his client that the securities they propose to issue are not required to be registered, but are bank securities and are exempt, and he's wrong. He's doing that in spite of the fact that the Division of Corporation Finance has already told the issuer (which looks like the Stanford International Bank, by the way) that they can't do this—that these are premium rate securities, that they are not adequately described and classified as exempt, and that under the *Ernst & Young v. Reeves* test, they resemble jurisdictional securities more than they resemble exempt bank notes, and are subject to '30 Act registration therefore – and they do prosecute Feldman.

There's a case involving a municipal bond lawyer. He is in possession of pretty clear information, if the facts are correctly recited, that would tell him that, in fact, the bonds do have arbitrage interest, that in fact, they're not really using the proceeds for what the proceeds will be used for, that they're investing them to get income on the proceeds. It's always been a concern of the bar that the facts recited in the consent decree may or may not be totally accurate, may overstate the violative conduct, understate exculpative conduct. That's true of all enforcement actions. It's true of Reg FD actions. There's nothing unique about the lawyers with this.

The point I'm making is I don't recall a checklist.[7] I do recall very careful discussion, a lot of discussion on where we had come in terms of elaborating this. If you look at the Don Feuerstein 21A report—in the famous footnote to the 21A report in the Salomon

[7] It may be that this arises under the Levitt Commission with Si Lorne.

Brothers Treasury report—there is a footnote that purports to trace where the snitch rule, where the reporting out by attorneys, has been sanctioned or required by state professional rules.

The Division of Enforcement, I'm sure, compiled that. I'm sure it was compiled to lend force to the idea that they were saying, they were announcing prospectively, that under the famous Brown, Wood case, the famous original case that spawned Ed Greene's comments on the scope of 102(e), that in fact, at some point, a lawyer who was a strategic decision maker had to withdraw. This was the Carter and Johnson case, in which the Commission says at some point the lawyer has to consider withdrawing. Ed Greene says those are going to be cases that are only brought if there's an underlying action against the issuer, and only if there's an injunction issued against the client. Ed Greene lays out in his famous New York Bar speech conditions to 102(e) proceedings. These erode. They are eroding.

It was felt that something had to be done when lawyers are, in fact, principal decision makers, part of the top rank of strategic planners in an organization, and they sit in meetings and they participate in these decisions, and they don't say, "Look, I think this is illegal. If we do this, I'm resigning." That's what the Feuerstein-Gutfreund case is about. It was a 21(a) report, just as the Carter and Johnson ruling had been prospective only. They had said, "we announce prospectively."

The Commission announced in the Feuerstein 21(a) report that people need to think about doing this. We think that attorneys can be liable under 102(e) if they don't disassociate themselves. Becomes very important in the Enron-Worldcom era. But there's no new legislation on it. Section 10(A) applies to accountants. I think, for good reason, the Commission has gone slowly in this area, and they have focused on cases where attorneys have actually done things beyond giving legally correct advice. That's the continuum. I think it's going to be interesting to see if there is further evolution in it. There's not a checklist. The closest thing you get to a checklist is the famous speech that Ed Greene gave, an article that I wrote, and then an article that Si Lorne wrote with Hardy Callcott.[8]

All of those are, to some extent, retrospective. Ed's is not. Ed's is setting out limits. All of the subsequent general counsels have been somewhat retrospective in looking back on where we've come. I think that's probably the appropriate function for the general counsel. It's to remind people where we've come. There's always suspicion in the bar that the chairman or the enforcement director wants to do a Rudy Giuliani or put a new mark on the wall. An Elliot Spitzer, Andrew Cuomo. That's the suspicion. There's tension there. I think the tension is probably creative, and I think that it depends on having balance. A much more serious threat, I think, is the actual statutory institutionalization and criminalization of conduct.

We've got to keep a balance between civil remedies, civil regulation of conduct, which continues to be considered important economically, and punishment. Clearly, there's a

[8] Which may have laid out a proposed "guide" or "checklist".

continuum. There is an outer limit where the conduct is criminal. And that's what *O'Hagan* shows, and it's what some of these more recent cases show. In the interim, there's a vast swath of conduct that may need to be checked by civil regulation that is not criminal.

KD: A number of times, you've mentioned the Salomon Brothers case.

JD: It was a big case for Richard. Huge case. He was tackling very important people.

KD: Tell me a little bit about the context. You would've been there about the time that that case came on, and followed it through.

JD: Well, first, it involved the market for Treasury notes. One might've argued it was at the margin of SEC regulatory authority.

KD: I think they did, didn't they?

JD: Yes. It involved very important people. People like Tom Newkirk and Joe Goldstein who are still around town and had to investigate and form the case are good sources of the dynamics. But I think the fact is that it was not a simple case. John Gutfreund had arguments, equities that were made in his favor, as did all of the others. There are very seldom cases in which egregious wrongdoing is found in one individual and nowhere else. The complexity of these cases involves the fact that most corporate decisions are decisions in an enterprise that involve more than one person, and that establishes a law-enforcement interest in a broader group of people, but it also makes the case more difficult to investigate, and complicates prosecutorial decisions when there is a conscientious intent by the government to do the right thing. The Salomon Brothers case was such a case.

KD: One of the issues which you've mentioned is this idea that the SEC was looking at treasuries. That was one of these instances where nobody was really taking responsibility. Was Richard Breeden interested in maybe establishing some precedent there and bringing under regulation something that had not been?

JD: Well, I think he saw the importance of the conduct in terms of the integrity of the markets and the transparency of the markets, and I think he was deeply offended at the notion that a firm thought it was big enough to corner a market, or to try to abuse a Treasury rule. One of the things we haven't talked about is mark-to-market reporting. In the mix of all of this, exerting pressure on the Commission, in addition to the remedies act, cease and desist, in addition to sanctioning attorneys, in addition to going after Salomon Brothers, in addition to trying to discipline people for entering false bids at the Treasury auction market, he also, of course, said, "First of all, we're not going to abandon GAAP. If you're Deutsche Bank and if you want to offer your securities and list them on the New York Stock Exchange, you'd better provide a footnote that reconciles your earnings and your reserves to GAAP." He, of course, was exactly right.

It was my job to go and talk to the New York Stock Exchange about it. It was one of the most interesting experiences I've had. By the way, Richard Grasso and Bill Donaldson performed great service for their country. They negotiated with Deutsche Bank a regime whereby Deutsche Bank could, in fact, list on the New York Stock Exchange, and the SEC could accept the financial statements because they reconciled German Reserve Accounting to GAAP. Government worked. Self-regulation worked. The Stock Exchange worked.

KD: But, of course, only a big guy like Deutsche Bank could get the New York Stock Exchange and the SEC to sit down—

JD: It was the important case. That was the important interest. But I think Richard Grasso and Bill Donaldson both saw that you'd have not only the Deutsche Bank, but Siemens, and it was important for all sorts, AXA and Allianz. There are all sorts of companies that would avail themselves of it once you can show them how it can be done. It was a source of great frustration to people like Ed Greene and others, which he articulated publicly and effectively, that something had to be done about this, that there was this huge well of investment that could flow into the United States if only we could solve this problem. Well, Linda solved the S-1 registration issue. F-20 became a very useful periodic reporting tool to carry them beyond the initial entry. And Richard Breeden and Bill Donaldson and Richard Grasso, the great trio of Breeden, Donaldson and Grasso, solved the accounting problem.

KD: You mentioned mark to market. Did this come out of the S&L crisis?

JD: Yes, it does. Because you had something called regulatory accounting principles. Regulatory accounting principles had been identified by everybody as having something to do with the failure of the system that had been in place to regulate the federally-insured depository institutions that were S&Ls. Richard very much believed in mark to market accounting and transparency. He believed that the volatility that occurred as a result of that transparency was better than the potential for serious misunderstanding and misstatement that occurred with historic cost accounting for financial instruments. He was in a very difficult position because he was also talking to Japanese, Mexican, European, and British regulators. Of course, the Japanese banking scandal was just about to come.

It didn't come immediately: The full dimensions of the Japanese banking scandal only becomes known, I think, after Richard leaves the Commission. But he was talking to them about what was building up, and people knew it. It was an elephant in the corner of the room that everyone knew was there. Richard made jokes about the fact that if someone wants to buy the ground that sits under the Imperial Palace and pay more than the entire market cap of General Motors and Merrill Lynch, they can do it. But do we believe that that's what the real estate is worth because that's what the Japanese banks are carrying it at?

He had wonderful crisp ways. In terms of somebody who has a crisp ability to target something like this, you've got Ronald Reagan and Barack Obama—it's hard to find anybody else that has been as crisp in expressing the dimension of an economic problem, or a complex accounting problem, but that was Richard's way of doing it.

It was a very serious issue. A very close friend of mine, a Rice classmate, a colleague and close friend, Robert Clarke, was Comptroller of the Currency. Bob had his own problems. He had the banks whom he regulated telling him, "You've got to stop this market-value accounting. If we do this, we have volatility and instability, and it will compound the S&L crisis."

There were arguments between the Office of Comptroller and the SEC, and I was on the front lines. Wonderful young treasury official named John Dugan who crops up, just happens to be the Comptroller of the Currency now, but John and I were in the middle of this. We were over at the Hill, and Kate Fulton and I would go over on behalf of the SEC, and John Dugan would come over with the woman who was then legal advisor to the OCC, Nan Archibald, I think. The four of us would meet, and we liked each other a lot. We became good friends.

We have become since then colleagues on the private side of the bar, but we have to go in and argue in front of Congressional committees these opposite sides of this position, and there would be these stormy sessions in which we would fight over legislation and drafting of proposed legislation that eventually found its way into the Remedies Act in

10A and other legislation. But the issue was not resolved. The importance of the issue now is another case of deferral, and I think it signifies the wisdom of something that Richard said, which is, "Let's do this now. We can do this now." Let's not wait until we have a financial meltdown to do this, another S&L crisis to do it.

Arguments can be made that that's not the reason we had the Bear Stearns collapse and the Merrill Lynch. All of that's true. It isn't the sole cause of our current financial problems. But, certainly, Congress is spending an awful lot of time arguing about what to do about it now, along with derivatives regulation.

KD: Right. But sometimes it's during the crisis that you can do things, rather than afterward when people are more willing.

JD: Not exactly. If you're a regulator (and I wouldn't have thought of this until I had a chance to serve at the SEC), that may be wrong.[9] If you're doing it when there's not a crisis, you may, in fact, be enabling regimes to be set in place that don't cause the crisis. You're swimming against the *Wall Street Journal*, and you're swimming against a lot of Milton Friedman. You're swimming against currents that were very strong and brought us great prosperity in the 1990s. These are not questions in which anybody should be pointing fingers and saying, "You shouldn't try to think that you are a Cassandra or an oracle in your own time, and that you were abused by not being listened to."

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[9] The Rahm Emmanuel maxim that a crisis should not be wasted is not the point, but whether you can't foresee and ameliorate the critics until the dimensions are known, may be false.

The point is: this uncertainty is what government's about, this is what policy is about. If you're fortunate enough, as I have been, to sit in some of these arguments, you develop a different view, and your view is, it is not possible to predict all of the unforeseen consequences, and it may well be that you will do some things that have bad unforeseen consequences, and some things you will do that are right. The one thing I think you can be sure of, and which Richard demonstrated he was good at, was not planning too precisely on what he was going to have to solve, and then only doing that.

Whether it's being chairman of the SEC or the president of a great university, or President of the United States, the problems that you're going to have to confront aren't the ones that you may necessarily have planned on confronting. They may not be the ones you're good at. What you'd better be ready to do is accept that that's part of the job, and accept that the criticism is going to go along with it, and that you're going to have to make some people angry. And you may be proven, in retrospect, in part to have been wrong. You may be shown to have been shortsighted in not doing something. I thought Breeden was spectacular at performing that, at knowing how to do that job. I think that Arthur Levitt was spectacular at it. They both had their critics.

KD: Did you talk transition at all at the point at which you decided to leave the SEC? Late December you said. At this point, you know there's going to be a new administration and all that stuff. Was your plan to stay for a brief period of time?

JD: No, Richard and I had had discussions about this. What I have told you is all part of the public record, or things you can get from the public record. I've tried to put it in context. I'm not going to tell you what the Chairman and I discussed about succession.

KD: That's fine. I was just kind of interested in whether you were looking at the election cycle and thinking, "Well, the SEC's going to maybe go in a different direction."

JD: No, no. I thought, first of all, the firm had been encouraging me to come back. It was wonderful that they wanted me back. I had felt that I should remember why I had come up here in the first place, and I had small children, I had accumulated debts. For all those reasons, it was time to come back to private practice. I had learned an immense amount, and I had met people and developed associations I could never have done, so I needed to be respectful of that. I knew that Richard would, eventually, leave. I didn't foresee how long it would be before they got around to finding a new chairman.

I think one of the things, by the way, that happened—I regard this as a watershed administration. It was not just the excitement of the time. The White House of George H.W. Bush had been clear that they wanted a corporate maven to be chairman of the SEC. They wanted Paul Volcker or Paul MacAvoy from Yale, people like that. They even said they talked to people. The late Richard Darman, I think, may have been deputized to go and find such people. Couldn't do it. Richard Breeden was chosen because he had been such a good friend of George H.W. Bush—he had done brilliant work for 41, he had been a good friend of Darman and Sununu, and others in the White

House, and Republicans on the Hill like Warren Rudman, not an easy task. Not something you do if you lack personal sensitivity. In other words, the characterization that Richard has the skin of an elephant runs out at some point. He's been pretty good at making people of very different kinds think he's a valuable friend and ally.

They came to him and said, "Why don't you go do it," and he did. At the end of his term, by contrast, there was no shortage of people who wanted to be Chairman of the SEC, and in Arthur Levitt they got a maven. Since then, everybody has wanted to be chairman. I'm not so sure how long that'll go on now, but everybody has wanted to do it. I think he transformed the attractiveness of the job. The results for the capital markets and the Agency have been totally good. Totally good. People can criticize what a given chairman may have done. You can't criticize the fact that the people they chose are, all of them, spectacular people with spectacular credentials.

They may not have foreseen the crisis they had to deal with. It is also clear to me that at some point early on, I was not at the Commission—I was handling enforcement cases when Bear Stearns broke. I do believe that if Chris Cox and Mike Halloran had walked over to the offices of Bear Stearns and said, "You've got a week to get your overnight credit capital balances up and your overnight cash commitments down. Do it in an orderly fashion, but get it down to ten to one, five to one," they would not have left the office before there would've been a call to the Hill, and they would've been summoned over, and people up and down, both sides of the aisle, would've been saying, "Who are you to tell these people how to run their business? You think you know more than the heads of AIG and Bear Stearns about what their capital ratios should be?"

There's a lot of hindsight, retrospective stuff going on about the fact that the regulators didn't react. The regulators didn't react. It's true. It's quite clear they didn't react. But if you read Alan Greenspan's *Age of Turbulence*, you get the clear impression that if they had reacted, there would've been a lot of people, including maybe the Chairman of the Reserve, who would have been all over them telling them they were wrong to do it.

KD: That's one of the insights that history gives you, is that things are not as easy as one assumes they must've been. Is there anything else that stands out that took place during your time that we haven't talked about?

JD: New offices created, Michael Mann. Richard wanted to invest the Office of the Chief Accountant and the Office of Economic Analysis with new vigor. There again, I think he had mixed success. The Office of International Affairs was a great success. The Office of Economic Analysis, he had mixed success with that. But in Henry Hu's new Division of Risk, Strategy, and Financial Innovation, you have the coming of that to fruition, and Richard, I think, would have liked to have been able to get something as robust on the ground, right on time. I think you do run out of time to do something like that.

I have mentioned the contribution Linda Quinn made to the Commission, but I believe it was clear that the two most brilliant people in financial services regulation at that time were Richard Ketchum and Linda Quinn. They were a matched pair of very strong intellects, wonderful advocates who complement each other and get the rest of the senior staff the right result. I think Richard Breeden was masterful at keeping them there and keeping that senior staff together and keeping it motivated.

KD: It sounds like that group was very important to him.

JD: I think so. Barbara Green became a source of terrific calm administration of the Chairman's office. Linda Fienberg did a terrific job of getting Richard settled. I think she was ready to go and do something else, and did. Jack O'Rourke and others were sources of advice and information to Richard. I had wanted to mention the work that he did with IOSCO. He started the Council of Securities Regulation of the Americas, and he really cut Mary loose and said, "Go do it," and she did it. If you were reading the details of the Argentine bank crisis, you might've seen the name of the young head of the Central Bank, who was forced out by Ms. Kirchner, Martin Redviodo.

He, of course, was one of the young regulators who first came to Richard's International Institute for Securities Regulation. Richard brought all these people up, sat them all down, had people come in and talk to them. It was tireless outreach and tireless proselytizing of the American securities markets' model of transparency, disclosure and market integrity. Some of those people have ended up as heads of central banks. And they have gone into places like Poland and done good things. Les Paga, who became the head of the Polish authority, eventually died tragically. Before he did, he put the Warsaw Exchange and Poland Securities markets on pretty solid founding.

KD: Did you go out on some of those trips?

JD: We went. I think we all thought that they were some of the most worthwhile trips we took, or some of the most worthwhile things we did. We went, and we met with people. I was in Beijing, and Michael Mann, Linda Quinn and Barbara Green were there. They were in a small meeting, and the Chinese brought in an entire staff of proposed securities regulators. One of these, Mr. Goa Xixian, has become an important guy in China, but they were all just young people at that time. The head of the agency was an old Communist Party pro who had been appointed. He knew how to start a meeting and sort of nod off in a meeting.

The meeting was really all of the staff members. And Richard, of course, observing strict protocol, did a lengthy presentation. Then he handed it over to Linda, and Linda spoke and participation sort of moved down the line. After the meeting, a number of these young Chinese women came up to Barbara, and to Linda, and they said, “You don’t realize what it means to us to have you here doing this.”

This was 1991 in the People’s Republic of China, and they said, “Oh, Ms. Quinn, Ms. Green, it means so much to have you doing this.” It was not without consequences that they were in places like Hungary, Mexico City, Warsaw, Moscow. I mean, the curtain was just down.

KD: Things were really in flux.

JD: The first time we went to Berlin, the city was just over being divided. And we spoke to people in Berlin whose children had moved from the east zone to the west zone, the west zone to the east zone, never expecting to see them again. Within weeks, the wall had come down. It was an extraordinary thing. I don't think that it was caused by the impending visit of the SEC! But I so think that the doctrine, according to the SEC, that was put out there was wholesome and pro-capitalist, and it is one that American capitalists would still be pretty happy with being put out, in retrospect.

KD: Well, that's all I've got on my list. I do note that you were involved with Fannie Mae and Freddie Mac, to some extent, way back then.

JD: Later. I met Peter Wallison, he was a young Treasury officer at that time. (Maybe he'd been a young treasury officer under Reagan, anyway he and Richard were pals, were friends.) We became concerned about what the GSEs meant (by way of systemic market risk).[10] Now we were, of course, pushing the aspirin up the Hill. We were trying to get to subjecting them to regulation under 12(g). We were trying, we were saying, "Leave the tax status alone, leave all that alone." We were missing the elephant. But Peter was not, Peter Wallison has seen this clearly from the first.

[10] Government Sponsored Enterprises

We were saying, "Look, a start would be to make them file annual reports, subject their annual reports and their accounting to Exchange Act liability." Here again, Richard, you would've thought he was Robespierre. He wanted to behead the heads of the GSEs. Of course, he was right. What they did, of course, was to come in and start filing the reports on a voluntary basis. That took away some of the steam of the argument. But they are financial institutions. If they had been subject to, perhaps, a little more current oversight of what they were doing with their accounting, it might've been avoided.

KD: And you may not have come back to them in a professional capacity.

JD: I might not have been there in 2003, 2004. I went over in 2003, our report was done by 2004. It became public, it was "techy", regulation and reporting of accounting. We were asked by Congress, "what about safety and soundness?" Richard, by the way, continually went to Congress and said there's no question but that the government securities markets, the municipal securities markets need more disclosure and more transparency. The government markets have tended to work pretty well, and the government-sponsored enterprises seem to have no safety and soundness issues that we can determine. That was, again, our message in 2003. Nobody on the Hill thought there were immediate safety and soundness issues.

Peter Wallison was not saying there were safety and soundness issues. He was saying that when the safety and soundness issues arise, it's going to pull them down like a house of cards. I don't think I'm doing violence. Peter can tell you whether I've forgotten one of his prescient articles. The first bad sign, I thought, was when our report came out, the *Journal* said it was riveting reading, it was all over Congress. We testified to the committees, and then they called in Frank Raines at Fannie Mae and they said, "What about this?" He said, "We don't have any of those problems. I've already checked with staff. We don't have any of them."

Sitting at home, I told Joan that I read that and my heart sank because I thought that was a CEO who has just done it: he's touched the bases with his financial officers and with his accountants and controllers, and they've said, "Oh, don't worry, boss, we don't have those problems." The problems were the advantage they took of the size of these enterprises to fall into accounting and bookkeeping practices that enabled them to disguise volatility, and that's wrong; but it's not the ultimate source of the current financial collapse. They were buying the wrong things. Their risk profile was unconscionably tilted.

In some cases, you wonder whether they knew. The statements that I'm reading now are that they were characterizing as good loans, loans that they knew fell outside the boundaries. I don't know whether this will ever be known. Maybe it's too late to get into it. But it shows you where a good friend of mine, Charles Niemeier, is right in that he says, "People don't set out to commit financial catastrophe and fraud. They sort of go along and it's the last step that they take." I think realizing the wisdom of that is part of the mission of the SEC. This is what Bill Donaldson was talking about when he's talking about trying to see around the corner. It's what Mary's doing when she puts Henry Hu in his division there. It is to try to anticipate where tendencies, trends are being established that have a bad last step.

If you want to look at one that Richard Breeden was talking about, or two that he was talking about, look at mark to market accounting, and look to GAAP and the principles-based accounting, and look at Mary, who's undergoing all these political pressures now, dealing with all these pressures, and what's she doing with IFRS? She's saying, of course, globalization is a fact of life: you can't be against harmonization, reconciliation and one uniform system accounting, but we're not there yet. We don't know what it is. Of course, she's right. They can't. They can't allow (or require) all companies to go to IFRS when there's Taiwanese IFRS and Milanese IFRS and Argentinean IFRS.

KD: I think that's a terrific place to wrap up. Thank you very much.

[End of interview.]