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THE SECURITIES AND EXCHANGE COMMISSION'S ADMINISTRATION OF THE SECURITIES ACT OF 1933 AND THE SECURITIES AND EXCHANGE ACT OF 1934

1. BASIC PROBLEM

The major difficulty is that the Commission has for years been deprived of any large objectives. It is engaged in no important program of improving corporate standards of morality. It has become almost exclusively a secondary police operation. The principal emphasis of the administration of the Acts has been on the number of administrative proceedings and prosecutions brought.

This fact has affected the whole administration of the Acts. It has resulted in all the evils which have to be combatted in a police force, e.g., subjective judgment as between good issues and "dogs"; between good brokers and bad brokers; the creation of black lists, and elaborate processes of both official and unofficial guilt by association.

Consequently, there is not even the semblance of fair and equal administration. All discretionary powers are openly used against what the staff has decided are the "bad" issues, the "dogs", the "untrustworthy" underwriters, in substance the "bad guys". The question of decision becomes not one of compliance with the Statute but whether investors should be allowed to invest in the issues, whether the price is too high or too low, or whether the underwriter is receiving too much compensation. All these are issues on which the staff is not competent (leaving the question of legality aside).

One other result of the failure of larger objectives and the emphasis on police operations is the tendency to select small companies and small underwriters as primary objectives of proceedings and prosecutions, the penalties imposed for similar infractions being inverse to the size of the company or broker involved. (This may be partly due to the fact that the small brokers and companies are financially unable to defend themselves against the attack of the Commission and that in most cases they have no choice but to succumb.) This has injured the Commission's reputation for fairness and has caused it to be widely criticized as an organization of small calibre.

The situation has been aggravated by the criticisms of the Harris Legislative Oversight Committee which attacked the Commission on the ground that it was not vigorous enough in enforcement, a charge not justified in the cases cited. Consequently, the staff, except when it is taking the most extreme prosecuting position, feels it may be subject to criticism by the Congress for not being vigorous enough.

2. SUGGESTED REMEDY

The return to larger objectives is in my view the most important affirmative task of the Commission. It will automatically reduce the police part of the operation to its proper proportions and simplify the problem of controlling and supervising personnel whose primary interest is prosecution.

There are many major projects which can enlist the enthusiasm of the present staff, and attract able personnel from the outside. I cite a few examples.

Proposals for important activities to be undertaken by the Commission.

1. Revival of the Commission's support (abandoned by the previous Administration) for the so-called Frear Bill to extend proxy rules, insider trading and other reporting requirements to larger companies not listed on exchanges.

2. Improving the standards of the various secondary Exchanges. Use of Section 19 powers to bring the standards of reporting, etc. up to the standards of the New York Stock Exchange which has, by default of the Commission, taken the leading role in securities reform in the last few years.

3. An inquiry and report on trading in the over-the-counter market - not limited to the kind of thing the N.A.S.D. has done with 5 per cent mark-ups etc., but a consideration of the nature of trading in the securities of established companies, costs to investors to get in and out, influences on the market, etc. This should be an inquiry to seek to formulate new rules and standards not an investigation to uncover violators.

4. A survey of the possibilities of facilitating listing of foreign - particularly European - securities on the American exchanges and the offering of their securities to the American public. The New York Stock Exchange has been active in this respect and some Commission officials are, of course, informed.

It seems appropriate to reassert the Commission's responsibilities and leadership in this field, e.g., by creating a special task force to investigate the problem and make recommendations.

5. Proxy regulations on inside dealings. So far as it is of consequence to the Commission's responsibilities, the Chrysler situation appears to require clearer and broader rules more than it requires investigation for wrongdoing.

There are many other ideas, of course, which can be and should be developed which will involve the Commission in problems of consequence requiring solution rather than the mere enforcement of a basically static code.

If the major deficiency is remedied many of the other problems will correct themselves. I think it appropriate now to mention some minor problems which I believe, nevertheless, to be of consequence.

1. <u>The delay in processing registration statements and Regulation A's.</u>

This is a major justified cause of complaint against the administration by the Commission. The backlog should be cleared up immediately even if it results in some issues being cleared in less than perfect form.

The Commission cannot defend itself against the charge that it has caused delay in financing to which issuers are entitled. It is justified in making only such examination as its personnel can make in a reasonable time.

The delay is in my opinion one of the major causes of short cuts, e.g., "private" offerings, "pledges", local sales, etc. of dubious legality.

Incidentally, I do not share the general view that the staff's "lint-picking" is a major problem. I do not believe that these minor items take much time of the staff nor of issuers. They may be annoying but issuers usually accept these comments without complaint and sometimes are very grateful for them. Of course, it would be a serious matter if the minor deficiencies occupied time which could be devoted to major matters, but I am inclined to believe this is not the case.

2. New Companies

One area in which speedy methods of handling and special techniques should be involved is the case of the first filing or the first substantial filing by new companies.

Special techniques should be evolved because normally these companies, represented by local counsel not specially familiar with S.E.C. regulations, are apt to require more intensive treatment. In general, this should be more sympathetic than it is today.

3. The Rules - small issues under Regulation A

These should be simplified.

(a) It should be possible to permit these to become effective rapidly without too much concern about detailed disclosure. Normally the issues involved are clearly speculative, financial statements show the facts and the generalized disclosure of a company situation could be handled very simply.

(b) Disqualifications from the use of Regulation A should be removed and there should be no suspension proceedings under Regulation A. The matters are too small for the cumbersome administrative machinery. If any case although small should be deemed

important, injunctive procedures are appropriate.

4. Enforcement

The Commission's emphasis should be more on litigation in the courts and less on administrative proceedings. There is no excuse for the normally long drawn out administrative proceedings. Nor is there justification for the supposed self operative consequences of the bringing of proceedings by the Commission itself -- e.g., temporary suspensions of Regulation A offerings.

If there is need for rapid action, injunctive process is always available and the Commission will get relief in every case in which it is entitled to relief as well as in borderline cases. This will not only improve the Commission's reputation for fairness but it will improve the calibre and experience of the legal staff. That staff, by and large, now participating only in proceedings before the Commission's examiners in their own offices, have little opportunity or need to test their proof, or exercise their persuasive powers. Consequently, their judgment as to whether or not they have a case and what reliance is to be placed in witnesses can be substantially improved by subjecting them to the necessity of presenting their cases to the courts. The effectiveness of administration will be improved in all ways, to the benefit of the reputation of the Commission and the skill of the staff.

It is sometimes argued that the Commission will be less able to secure its objectives in the courts. If so, this is because its objectives deserve to be limited. My own observation is that in

every situation where the Commission has presented a tenable argument, the courts have a very strong tendency to favor it (even more so than is the case with most government agencies.)

5. Administrative Proceedings

Where administrative proceedings involving a factual issue are necessary (which they sometimes are), the whole procedure should be revised. The present rules give the staff power to initiate and control the proceedings without any supervision by the Commission itself and very little by the examiner. The Rules should require equality between parties. Since the Commission is undoubtedly too busy to do the job itself it should use the hearing examiners for a large part of this work. The hearing examiners should be given power to compel specification of charges, to limit issues, to conduct pretrial negotiations and to compel the conduct of proceedings on a basis similar to that of a civil case under the Federal Rules with, among other things, discovery rights to the respondents. This would require reeducation of the examiners to a much larger role than that to which they have been accustomed.