

EDWARD J. MARKEY, MASSACHUSETTS CHAIRMAN

U.S. House of Representatives
Committee on Energy and Commerce

LAWRENCE R. SIDMAN
CHIEF COUNSEL AND STAFF DIRECTOR

SUBCOMMITTEE ON TELECOMMUNICATIONS AND FINANCE

Washington, DC 20515

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The Honorable David S. Ruder
Chairman
Securities and Exchange Commission
450 5th St., N.W.
Washington, D.C. 20549

Dear Chairman Ruder:

This letter is intended to elicit further clarification of the Commission's views concerning former Commission Chairman John S.R. Shad's planned assumption of the position of Chairman of the Board of Drexel Burnham Lambert Group, Inc. It follows the receipt of the May 2, 1989 letter on this subject from Commission General Counsel Daniel L. Goelzer, which in turn was a response to my line of questioning at the April 19, 1989 Subcommittee hearing on the Commission's authorization request for Fiscal Years 1990-1992.

Mr. Goelzer's letter reiterates your hearing testimony that there is no statutory or regulatory bar to Mr. Shad's employment at Drexel. The Subcommittee never suggested that there was any such bar on employment per se. Rather, we focused upon the lifetime restrictions in 18 U.S.C. §207, which would prohibit Mr. Shad from representing Drexel in dealings with the SEC in connection with any "matter" in which he participated personally and substantially while he served as Chairman of the SEC.

Mr. Goelzer's letter correctly interprets the term "matter" in the context of the Drexel proceedings to extend to certain events, deliberations and determinations which may occur subsequent to approval of the settlement decree. In particular, on page five of the letter Mr. Goelzer states:

I do recognize that there may be some aspects of the implementation of the consent decree which are so closely related to the underlying investigation that Mr. Shad should not be permitted to act as Drexel's representative or advocate before the Commission concerning them. Similarly, there may also be other proceedings pending now or initiated in the future, which are intertwined with the Commission's case against Drexel. Such related

proceedings would include investigations and suits brought by the Commission or the U.S. Attorney against present or former Drexel employees and suits by private individuals or corporations involving the same (or closely-related) facts which formed a basis for the Commission's action against Drexel or which were found during the investigation for which Mr. Shad voted. In addition, the settlement agreement recognizes the possibility that it might be terminated in the event that certain contingencies occur; in that event, Drexel and the Commission would find themselves again in litigation. In these situations, Mr. Shad would be precluded from representing Drexel before any federal agency, or advocating a position to the government, concerning the matter in question.

Mr. Goelzer's letter notes that "aspects of Drexel's future business will be governed by the terms of the resulting consent decree," by which I am sure he is referring to the settlement's mandate for an extraordinary level of future Commission involvement in the oversight of Drexel's business. This includes restrictions on future trading practices by Drexel employees, personnel decisions, and the structure of the firm's high-yield bond operation. The agreement foresees intensive scrutiny of Drexel's future operation by the Commission's independent auditor, with the possibility of the initiation of Commission administrative proceedings in the event of any serious failure in Drexel's compliance.

Given the future need for extensive discussions between the Commission and Drexel in implementing the agreement, and the overwhelming likelihood that at least some of this implementation will involve the same "matter" as the original Drexel investigation which Mr. Shad initiated, Mr. Goelzer proposes to prepare "written guidelines" which will detail the necessary post-settlement limitations on Mr. Shad's activities at Drexel. Mr. Goelzer proposes that these guidelines be prepared only after the entry of the final decree in the case.

I have several concerns with regard to these written guidelines and the timetable for their preparation. First, why should their preparation be delayed until after the entry of the final consent decree? In response to questions at the April 19 hearing regarding the propriety of permitting current Chief Executive Officer Fred C. Joseph to remain in place at Drexel, you responded that despite "some concern" with that question, the "most significant aspect of the change in culture [at Drexel] will take place...by Chairman Shad being there." Yet, Mr. Goelzer's letter acknowledges that Mr. Shad will now be precluded from

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discussions with the government concerning some aspects of the agreement's implementation as well as any future related Commission proceedings against Drexel personnel, including those at the highest levels. Given these facts, and the need to provide Drexel with fair and timely notice of restrictions on Mr. Shad's future activities and the court with assurances of his effectiveness in maintaining an effective supervisory role there, what is the rationale for not submitting the Shad "guidelines" to the court in advance of its consideration of the settlement?

Another concern arising from Mr. Goelzer's suggested approach is his view that the development of these guidelines "will necessarily entail discussion with Mr. Shad." I have serious concerns about the propriety of the individual who is subject to lifetime post-employment restrictions under 18 U.S.C. §207 actually negotiating over the substance of those legal restrictions. Furthermore, because such discussions themselves go to the heart of the implementation of the settlement agreement, I would question whether Mr. Shad's participation would not be inconsistent with the Commission's decision to exclude Mr. Shad from all pre-settlement negotiations with Drexel. Please provide a rationale for this decision to permit Mr. Shad's participation in the design of the written guidelines. Furthermore, please provide any precedent for a subject of post-employment restrictions negotiating over the substance of those restrictions.

In summary, Mr. Chairman, let me express my support for your efforts in the investigation, prosecution and settlement of the case against Drexel. Nonetheless, I am obliged to ensure that the letter and spirit of the conflict of interest laws governing the future activities of Mr. Shad as the Chairman of Drexel are scrupulously observed. I request that you respond fully and completely to the questions and requests set forth above, no later than Monday, May 15, 1989. Should your staff have any questions concerning this request, please have them contact Howard B. Homonoff of the Subcommittee staff.

Thank you for your cooperation in this regard.

Sincerely,


Edward J. Markey
Chairman