

SECURITIES AND EXCHANGE COMMISSION HISTORICAL SOCIETY

THE ROUNDTABLE ON ENFORCEMENT

Wednesday, September 25, 2002

2:00 p.m.

William O. Douglas Open Meeting Room.
U.S. Securities and Exchange Commission
Washington, D.C.

ATTENDEES AND PANELISTS:

Theodore A. Levine, President
Securities and Exchange Commission Historical Society

Hon. Harvey L. Pitt, Chairman
U.S. Securities and Exchange Commission

PANEL ONE:

Irving M. Pollack, Co-Moderator
Stanley Sporkin, Co-Moderator

Theodore Altman
Thomas Rae
Richard H. Rowe
David Silver
Theodore Sonde

PANEL TWO:

Irving M. Pollack, Co-Moderator
Stanley Sporkin, Co-Moderator

David P. Doherty
Benjamin Greenspoon
Theodore A. Levine
Alan Rosenblat
Theodore Sonde
Wallace L. Timmeny

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MR. LEVINE: Good afternoon. I am Ted Levine. And as President of the SEC Historical Society I would like to welcome you to our third Oral History Roundtable. It is going to be a roundtable on enforcement.

I would like to thank the SEC for their continued assistance in helping the Society to present the history of the Commission and the securities industry. For the first time the Society is broadcasting the roundtable live on our website. So I welcome all Society members and friends who are listening at this time.

I invite all of you to visit the virtual museum of the SEC Historical society on our website which is www.sechistorical.org to see past roundtables, listen to oral histories, read original historical records and papers and see some great old photos all relating to the history of the Commission. The museum is available free of charge on the website 24 hours a day, 7 days a week. Each month we add new materials. And this roundtable will be online in the next several months.

I would like to thank three persons who have helped make this roundtable today possible. Alan Levenson, the Chair

1 of our Oral Histories Committee since its inception who is
2 unable to be with us today but has really been the driving
3 force behind these oral histories. Carla Rosati who is
4 sitting here, the Executive Director of the Society, who
5 actually is the person who put all this together. And third,
6 Dan Hawke who is with the SEC Division of Enforcement and a
7 member of the Oral Histories Subcommittee who did a splendid
8 job in preparing the paper on the history of enforcement which
9 is in your program and outside for your reading pleasure.

10 The Society is beginning to form operational
11 committees for each of the major divisions of the SEC, the
12 Chief Accountant's Office, the General Accountant's Office,
13 the regional offices and the Commission itself. Each of these
14 committees will help to identify and secure material for our
15 museum as well as to host programs and activities relating to
16 their specific area.

17 Steve Cutler will be here, the Director of the
18 Division of Enforcement, and will be coming later. And in
19 order to keep on schedule with Irv and Stanley looking at me
20 this way I would like to now introduce Chairman Harvey Pitt.
21 Harvey was a founder and past president of the Historical
22 Society and has agreed to say a few words before we start the

1 roundtable.

2 Chairman Pitt.

3 (Applause.)

4 CHAIRMAN PITT: I know everything us all right when
5 Carla is here.

6 Let me say that I am proud to welcome all of you to
7 today's Roundtable on Enforcement. And it's an introduction -
8 - it's an honor to introduce two people who need no
9 introduction, Irv Pollack and Stanley Sporkin.

10 Before I do, I had a meeting yesterday with some of
11 the folks in our Pacific Regional Office. And Sandy Harris
12 who as you know is in charge of a lot of our enforcement work
13 out in L.A. gave me personally a copy of the 1938 SEC
14 Enforcement Manual. This is a manual that was issued when
15 William O. Douglas was Chairman and Messrs. Mathews, Healy,
16 Frank and Hanes were on the Commission. And what I thought I
17 would do is turn this over to Ted for the Historical Society's
18 archives. It's really fascinating. It's a great piece of
19 work.

20 I think you know that Irv joined the Commission's
21 most distinguished office, its General Counsel's Office, in
22 1946 after having served in the Armed Forces during World War

1 II. And 15 years later Judge Sporkin joined the SEC as an
2 attorney working on the Special Study. Most people think that
3 Irv and Stanley are joined at the hip, and they are to some
4 extent, but there was this 15-year hiatus.

5 Both Irv and Stanley were instrumental in making
6 the Commission and the Division of Enforcement what it is
7 today which I think is one of the most highly regarded
8 governmental enforcement programs, and deservedly so.

9 As I think you will be able to tell today, Irv and
10 Stanley in addition to being joined at the hip have worked
11 together for a long time. Prior to the creation and running
12 of the Division of Enforcement Irv was the director of what
13 was then known as the Division of Markets and Trading,
14 actually it's Trading and Markets, and Stanley was his deputy.

15 At that time their division housed much but not all of the
16 Commission's enforcement program. Pieces of it were scattered
17 around in the regulatory divisions as well.

18 Eventually the enforcement function was split off
19 from trading and markets. And today we have a Division of
20 Market Regulation and the Division of Enforcement. In August
21 of 1972 Irv became the first Director of Enforcement. And in
22 1974 Stanley succeeded him when Irv was appointed to the

1 Commission.

2 If I am not mistaken, Irv, I think you were the
3 first, maybe the only director of the Enforcement Division who
4 ever served on the Commission.

5 Irv, of course, helped establish the Commission's
6 credibility with other regulators through his meticulous work
7 habits. For example, Irv used to read every reported criminal
8 case. And he developed an extensive card file of case notes.

9 For those of you who don't recall, in the old days we used to
10 have a criminal reference process and it was quite an involved
11 project to make a criminal reference. Somehow over the years,
12 and particularly even after the Fields case we found easy ways
13 to make those references.

14 In any event I would say both Irv and Stanley share
15 zero tolerance for corruption and their attitude serve the
16 investing public well. Together they built a national
17 enforcement program with a reputation for integrity,
18 tenaciousness, fairness and creativity. And looking back at
19 the problems that Irv and Stanley took on such as off-the-book
20 transactions and corporate accountability it is somewhat
21 striking that those issues seemed similar to challenges we at
22 the Commission are facing today. And that's why today's

1 program is really quite timely and relevant.

2 Stanley delivered a speech in which he said the
3 following:

4 "What I find," -- I can't do it the way Stanley
5 would do it -- but "What I find particularly troubling in the
6 attitude of corporate executives is the extent to which they
7 define their responsibility to shareholders only in terms of
8 the bottom line. They are willing to disclose the amount of
9 their company's earnings but not the manner in which those
10 earnings have been achieved. They attempt to argue that
11 shareholders are not interested in this information despite
12 its reflection upon the quality of the company's earnings and
13 management."

14 Now, I'm sure you all remember that this was, these
15 words were uttered by Stanley at the UCLA Dean's Forum in Los
16 Angeles on January 15, 1976. I have to say, Stanley, I don't
17 even know why I bother writing new speeches, I mean I could
18 just recycle the things you've already said.

19 In any way, in any event I think that Irv and
20 Stanley continue to be influential as leaders of the
21 securities bar. The Commission and the public can always look
22 to Irv and Stanley as honest brokers on any issue. And it is

1 a privilege to have them here today.

2 I also want to take a moment to publicly
3 acknowledge the pro bono project that Stanley undertook at my
4 request in reviewing our administrative process. It is my
5 fervent hope that we will completely revitalize and revamp the
6 administrative process creating the equivalent of a rocket
7 docket so to speak. And Stanley wrote a report on this that
8 is just absolutely phenomenal. And for those of you who
9 haven't seen it we posted it on our website so it's available.

10 I would also like to thank the SEC Historical
11 Society for putting together today's program. Our agency has
12 a strong sense of history and through programs like these the
13 Historical Society helps us to learn and understand that
14 history. Euclid called history "philosophy teaching by
15 examples." And I can't think of any better examples to teach
16 us than Irv and Stanley and the panelists we have assembled
17 here today.

18 I would also like to take a second to recognize
19 Daniel Hawke who is an attorney in our Enforcement Division.

20 The Roundtable has outside a summary of highlights
21 for distribution that Daniel prepared. And his summary turned
22 into a 41-page history of enforcement at the SEC completed

1 with 216 end notes. I think Daniel deserves a lot of
2 recognition for what he's done and we're very appreciative.

3 (Applause.)

4 One of the reasons why I think it's so important to
5 take a moment now to recognize what Dan has done is that
6 today's staff are tomorrow's panelists. And people like Dan
7 continue the tradition that Irv and Stanley helped establish
8 in the Division of Enforcement, vigorous protection of
9 investors and then spreading the message.

10 And so now I would like to turn the program over to
11 Irv and Stanley.

12 PANEL ONE

13 MR. POLLACK: Thank you, Harvey, for your very
14 gracious remarks on behalf of the panel and Stanley and
15 myself.

16 I would like to start off by just mentioning one
17 program in the old days that was principally a regulatory
18 program but also had enforcement aspects to it. And that was
19 the Public Utility Holding Company Act of 1935. It was
20 referred to in those days by the opposition as the death
21 sentence for public utility companies.

22 It turned out after the innovative and imaginative

1 enforcement by the then SEC staff to be the savior of the
2 public utility industry. And in a few years, using voluntary
3 cooperation from the companies, it restored these completely
4 devastated companies into the blue chips that we knew for many
5 years.

6 And with that brief introduction I will let Stanley
7 have the first question.

8 MR. SPORKIN: All right, folks, let's throw up an
9 easy one.

10 Division of Enforcement, you people all had you own
11 little enforcement programs. Good or bad idea to consolidate
12 enforcement into one division? What do you think, Richard?

13 MR. ROWE: I think history has proven that it was a
14 good idea.

15 MR. SPORKIN: What did you think at the time?

16 MR. ROWE: I wasn't quite sure at the time. You
17 know, the expertise that the Division of Investment Management
18 had in their enforcement program, that we had in our
19 enforcement program and business, corporate finance --

20 MR. SPORKIN: Right.

21 MR. ROWE: -- had something to be said for it. But
22 if you stop and think, each of us had only limited authority.

1 The Division of Enforcement has authority to refer things
2 criminally, to go into court and prosecute any kind of civil
3 case that the Commission is authorized to prosecute. And we
4 didn't have that broad authority.

5 Now, there is something to be said for centralizing
6 the enforcement in one division. You get more consistency
7 that way. You get a, you also get a Stan Sporkin and an Irv
8 Pollack heading it up which also has been helpful.

9 MR. SPORKIN: Well, Ted, what do you think? You
10 were an investment man -- what happened prior to the Division
11 of Enforcement which was created in '72 each of the divisions
12 had their own enforcement. The first part of our panel is
13 going to consider those people that had enforcement programs
14 outside the Division of Enforcement. Of course, Ted, you
15 later came in. So you can now give your view both having your
16 own enforcement program in the Division of Investment
17 Management and then coming to the Division of Enforcement.

18 MR. ALTMAN: I think it worked out extremely well.
19 I'm not sure if it was designed to work out the way it worked
20 out. It increased the resources available for investment
21 management and better integrated the enforcement programs of
22 the divisions with each other. I think it enhanced the

1 Division of Enforcement as well as enhanced the investment
2 company, investment advisor enforcement program.

3 MR. SPORKIN: Tom, let me ask you this question:

4 You served in the Division of Trading and Markets
5 at the time. You were not here I remember when the Division
6 was formed. What would you have done if the Chairman came to
7 you and said, Hey, we want to have, we want to consolidate it
8 in one division? What would you have done?

9 MR. RAE: Well, as you recall, Stanley, I started,
10 and probably the only one here who started in the San
11 Francisco Regional Office. And I served there for three years
12 from '57 to '60 and then came back to the Division with
13 President Kennedy's inauguration. No, I would have been for
14 it. But I think I saw the reformation and the renaissance of
15 enforcement take place in 1961 and '62.

16 When I came back to the Commission in 1960 the
17 Enforcement Division was a pretty sad sack of characters I'm
18 afraid. It wasn't proactive at all. It was reactive. A lot
19 of old thinkers. The best talented attorneys wanted to work
20 in other divisions. Enforcement was thought to be the bottom
21 of the heap as far as getting a job.

22 But when Ralph Saul started the revolution and when

1 he brought Irv Pollack down from the Office of General Counsel
2 we saw a real renaissance in morale, on new attorneys, on a
3 different attitude and what have you. And at that time, and I
4 think in the next six or seven years I mean we just thought we
5 were the best. And with the proper talent I would have loved
6 to see a merger of all enforcement activities in one division.

7 MR. POLLACK: Ted, you ought to comment because you
8 were in the General Counsel's Office and I think you had an
9 oversight.

10 MR. SONDE: Well, I used to serve, I was in the
11 General Counsel's Office slightly after Irv left and saw the
12 enforcement more as a service arm for what I did. I mean I
13 used to handle those cases. And a lot of the cases were
14 scattered. And, frankly, I don't think that you could have
15 the program that you did have if the divisions and the
16 enforcement programs were scattered the way they were.

17 There wasn't a cohesive program. There wasn't
18 someone to plan and execute. You had people in four or five
19 different groups who each had their own constituencies. And I
20 don't think it would have been nearly as effective if it had
21 stayed in the disparate form that it was.

22 MR. SPORKIN: Let me ask, and I will throw this up

1 to anybody. And probably you, Irv, would know the answer.
2 How did it happen? I mean this wasn't because -- we all now
3 see what were the consequences were but what was behind it?
4 This is what a historical society is all about. Was it all
5 good motives or were there some not so good motives to create
6 the Division of Enforcement? Some people are thinking that
7 you might have been a little too tough there, Irv, and they
8 were trying to send you to Coeur d'Alene, Idaho or something
9 if they had an office up there.

10 MR. POLLACK: No, I don't think it was because I
11 was too tough in the enforcement area. I think it was more in
12 the regulatory area.

13 MR. SPORKIN: Yeah.

14 MR. POLLACK: I think there was a feeling that
15 perhaps the Enforcement Division was too overpowering in
16 determining the regulatory policies.

17 MR. SONDE: Irv, I always thought that you were
18 transferred out of Trading and Markets because there was an
19 antitrust concern and they figured that the best way to get
20 you out of the marketplace was to move you over to enforcement
21 so you wouldn't be jockeying with the Antitrust Division about
22 the stock exchange.

1 MR. POLLACK: Well, that later came in.

2 MR. SPORKIN: Yeah.

3 MR. POLLACK: But that's a different story.

4 MR. SPORKIN: Yeah.

5 MR. POLLACK: But getting back to what Tom said, I
6 think that Chairman Cary recognized when he came in that there
7 wasn't a viable national enforcement program. And so it was
8 his thought to transfer me with my criminal reference
9 responsibility that I took as assistant general counsel from
10 the General Counsel's Office to the Trading and Exchanges
11 Division, as it was then known, to take up the enforcement
12 program which Ralph Saul had started but was then over in the
13 Special Study.

14 So that I think the only thing that you lose when
15 you separate, for example, regulation from enforcement was the
16 symbiotic relationship that we had in the division so that
17 when we had enforcement issues or programs that we saw and
18 took action we could at the same time direct the regulatory
19 people to take steps because enforcement, like law, is the
20 last resort.

21 Your regulatory program and your disclosure
22 programs are really the basic foundation of your statutes.

1 And Stan and I tried to use the enforcement program not only
2 to take care of the egregious violators and put them in jail
3 but also to use the civil and administrative remedy to create
4 in the marketplace a feeling that it was to your benefit and
5 the long interests of the success of your institutions to obey
6 and respect the laws because they would help you do a quality
7 business that would satisfy your customers, the investors, for
8 whom all these statutes were enacted.

9 Stan, you can probably add something on your access
10 theory --

11 MR. SPORKIN: Yeah.

12 MR. POLLACK: -- in terms of that program.

13 And then, Dave, you can.

14 MR. SPORKIN: Well, Dave wants to.

15 Let me ask you this question then you can add what
16 you want to add.

17 Special Study was a fantastic effort. Did the
18 Special Study at all address the subject of enforcement? And
19 if not, why not?

20 MR. SILVER: Not directly. I think the Special
21 Study's impact on enforcement was really the creation of an
22 encyclopedic store of knowledge and knowledgeable individuals

1 who then later were able to take that information and put it
2 to use wherever they were in the Commission.

3 But to go back a step, you asked the question of
4 how did it come about? I think Irv put his finger on it when
5 he said that Chairman Cary was not only the symbol but the
6 potent force behind what had happened. But there is always
7 the old argument do events make the man or does man make the
8 events?

9 Well, in the early '60s and late '50s was an
10 enormous period of transition in the economy. The markets
11 were becoming national as they never had before. So the
12 regional offices of the Commission were becoming rapidly
13 obsolete whether they knew it or not. And there had to be a
14 change sooner or later to a national program.

15 I would not be quite as harsh as Tom was on the
16 inhabitants of the Division when he came there. I came in
17 1960 also. I think the bureau or Office of Enforcement in the
18 Division of Trading and Exchanges did what they were supposed
19 to do. They acted as a service agent for the regional office
20 processing papers.

21 When Ralph Saul came to the division and he saw
22 problems in the marketplace, etc., I think he also saw, shared

1 Irv's views who was up, then up in the General Counsel's
2 Office, that enforcement had to achieve a national posture.
3 Ralph was very wise in this respect, he did not take on the
4 established bureaucracy directly, he bypassed it. He set up
5 task forces to handle specific large cases and drew on the
6 resources of the Division to handle those cases.

7 It was almost a free form period as far as
8 enforcement was concerned because Ralph ran a very non-
9 hierarchical shop. That can be a lot of fun, it can also be a
10 lot of frustration involved. But that's the way Ralph ran the
11 division.

12 And I think with the revival of the interest in
13 regulation by Bill Cary who very shortly after his arrival
14 wrote the decision in the CaDy, Roberts case and then the
15 activity referrals in the General Counsel's Office and the
16 activities of Ralph bringing large enforcement cases in the
17 Division led to a de facto centralization of enforcement long
18 before it was actually embodied in any Commission order.

19 MR. SPORKIN: All right, let me ask you this
20 question, folks. In your divisions where you operate how was
21 enforcement policy created? Did it come from the staff or did
22 it come from the Commission? In many agencies that we see

1 operating in this town that the staff waits until the
2 commission tells them what to do. Was that the case, for
3 example, Corp. Fin., did you and Alan generate the program or
4 did you wait till the Commission told you what to do?

5 MR. ROWE: No, we didn't, we didn't wait for the
6 Commission to tell us what to do. I remember one time Manny
7 Cohen tell Al Levenson that he didn't want any bad cases. But
8 other than that we really didn't have direction from the
9 Commission.

10 (Laughter.)

11 I'll give you an example. For many years the only
12 thing that Corporation Finance could do was bring to a stop
13 order proceeding which is to stop the registration statement
14 from being effective. Wouldn't really have to have real time
15 enforcement because once you started the proceeding the
16 offering couldn't go forward. But we weren't touching '34 Act
17 reports. And then Frank Wheat came out with his study and
18 emphasized the importance of '34 Act reports.

19 We found a provision in the statute, Section 15 (c)
20 (4), that allowed the Commission to institute administrative
21 proceedings against '34 Act reports. We convinced the
22 Commission we could also go to court and sue to remedy

1 delinquent filers. And so we concentrated on the '34 Act
2 whereas in the past it had been only a '33 Act statement.

3 That came from the staff, not from the Commission.

4 MR. SPORKIN: And that was something that came
5 about through your discussions with Alan and the --

6 MR. ROWE: Right.

7 MR. SPORKIN: -- people on the staff.

8 Tom, what about you, would you sit around waiting
9 or did Irv tell you what to do?

10 MR. RAE: Well, I think it was a little bit of
11 both. I think Chairman Cary did have an image that --

12 MR. SPORKIN: Yeah.

13 MR. RAE: -- the division's function had to change.

14

15 For one thing, the regional offices were so
16 undermanned they couldn't undertake large investigations that
17 really used a lot of manpower or multi-regional in aspects.
18 And for the first time a headquarters office itself organized
19 a special investigative unit. We took on the boiler rooms in
20 Washington, D.C. and we took on cases wherever ---

21 MR. SPORKIN: The boiler rooms in Washington, D.C.?

22 MR. RAE: Washington at one time was full of human

1 boiler rooms.

2 MR. SPORKIN: Oh, my gosh.

3 MR. RAE: At the same time that Irv was there once
4 we were given the authority and the range and the
5 encouragement I think it came a bit of both, of things we
6 thought should be done, we should be proactive and what have
7 you. So I think it was both a combination of both the staff
8 itself and the Commission. It was just a new atmosphere
9 created, all to the good I must say.

10 MR. SPORKIN: Ted, was it you or Saul or who?

11 MR. ALTMAN: As far as I could see when I got there
12 in 1967 it all came from the staff. First of all, the
13 investment companies and investment advisors were nowhere near
14 the force in the industry that they are today.

15 And to the extent that issues developed, and this
16 is one of the I think usefulness of putting all enforcement in
17 one area, to the extent that issues developed there tended to
18 be overlaps and sometimes different perspectives. For
19 example, the big issues of the day were, they're still around
20 today, whether or not people have conflicts and are properly
21 using brokerage in transactions or other aspects of industry
22 activity.

1 We had such fundamental issues as how do you value
2 unmarketable securities? Until the late '60s there were no
3 real guidelines around for how a mutual fund or any other
4 organization might value restricted securities. And the
5 scandals would come about with somebody who'd buy a small
6 company stock in a private placement for a couple bucks. The
7 fact of the acquisition would turn that \$2 stock into a \$20
8 stock and all of a sudden you have a hero on Wall Street.
9 Those types of conflicts, brokerage, valuation come up in
10 different forms today.

11 But what happened, those issues all came from the
12 staff, there wasn't any direction I saw coming from the
13 Commission.

14 MR. SPORKIN: Ted, you probably are the person that
15 was most responsible for this get tough with the
16 professionals, well I guess Irv and you, but was that
17 something that was a creation of the staff or was that
18 something that the Commission called you up one day and said
19 go after those S.O.B.'s in the accounting profession and the
20 legal profession?

21 MR. SONDE: I think, Stanley, with very few
22 exceptions the initiative throughout the Agency was at the

1 staff level. There were very few situations where the
2 Commission initiated anything.

3 I think that the initiative with respect to the
4 professionals came from the staff. And I think I only played
5 a small part in that because there was a high level of
6 frustration at the staff both in seeing the accounting
7 professional fall down on its job and the legal profession
8 essentially aiding fraudulent schemes of one sort or another.

9 And --

10 MR. SPORKIN: Well what was this, this was
11 yesterday; right?

12 MR. SONDE: No, this was 30 or 40 years ago.

13 MR. SPORKIN: Are you kidding me? That was 30 or
14 40. Then what are we talking about today?

15 MR. SONDE: I remember, Stanley, the frustration of
16 some of us trying to work with a fellow who was just a
17 loveable character named Andy Barr who was the chief
18 accountant and trying to convince Andy to let us bring our
19 first case against a major accounting firm.

20 And then after that there were a series of cases
21 and he was joined -- he was succeeded by Sandy Burton. And
22 Sandy Burton helped us bring I want to say 12 to 15 major

1 cases against accounting firms. And I remember when Corp.
2 Fin. brought me the National Student Marketing case and we had
3 to decide whether to go after the lawyers or not. And Allen,
4 who is not here but played a major role in that, and Dick, we
5 debated whether or not we could do that. And the big question
6 was could we get it past the Commission?

7 At that time Bill Casey was the Chairman and he was
8 surrounded by a number of people who had just come from large
9 Wall Street firms and frankly didn't think we could get it
10 past the Commission. To our surprise there was no dissent
11 from the Commission and it sailed through but.

12 MR. POLLACK: You know, you mentioned Andy Barr,
13 the accountant. The opposition by the chief accountant
14 resulted in the first indictment of accounting personnel in
15 the Continental Vending case. The U.S. Attorney who was
16 presented with the chief accountant's views as to the
17 responsibilities of accountants was shocked and said if that's
18 what the accountants' position is maybe we have to indict
19 them. And they did. And two of them were subsequently
20 convicted.

21 So the criminal reference program served a great
22 function in centralizing all of the Commission's enforcement

1 activities because that was the one service that was
2 concentrated initially in the General Counsel's Office and
3 then in my role in the Trading and the Markets Division. And
4 we used that service because of the shortage of our personnel,
5 to get a great hit for the time and effort we put into those
6 cases.

7 Of course, we then had the U.S. Attorneys' offices
8 around the country, but principally in the Southern District
9 of New York, to bring our enforcement cases. And once they
10 understood how good our cases were, and how important they
11 were and how valuable they were to their offices in increasing
12 their reputation in the white collar crime area, we had a
13 symbiotic relationship where they would open their functions
14 and their people to us, particularly in major cases we could
15 really accomplish something in the national enforcement
16 program that we had.

17 MR. SPORKIN: David?

18 MR. SILVER: Irv, did the Commission ever distill
19 from the literally hundreds of enforcement cases involving
20 accountants anything from those cases and feed it back into
21 its regulatory program or did those cases really from the
22 Commission's and the public's point of view all turn on what

1 you might call a bad guy theory of history that there was one
2 bad guy and that was really the problem in the picture, not
3 weakness on the auditing side?

4 MR. POLLACK: Because of the opposition of the
5 Chief Accountant's Office to regulation of the accountants
6 Stanley and I had to bring cases against the accounting firms,
7 not against the individuals but against the accounting firms
8 on the theory that that would get their attention and that
9 they would then do a self-compliance program.

10 And for a period of time it did work consistent
11 with the overall philosophy that I mentioned much earlier in
12 my comments.

13 MR. SPORKIN: I think what happened was that it was
14 probably under control at that time. It got out of control
15 when a Commission decided that you don't sue accounting firms
16 anymore, you sue bad accountants or you sue bad brokers. And
17 I think that, that caused a bit of a problem.

18 But, David, let me ask you as the philosopher here,
19 what do you think of the balance between where these ideas
20 ought to generate from? Should it come from a Commission who
21 is put on by the President with confirmation or should it come
22 from unelected, unconfirmed staff members? Where should it --

1 MR. ROWE: You're leading the witness, Stanley.

2 MR. SPORKIN: Well, I'm asking which way.

3 MR. SILVER: I'm not sure where he's leading me.

4 MR. SPORKIN: I think in 14 years I'd learn how to
5 answer a question that wasn't a leading question. I'm saying

6 --

7 MR. SILVER: Only 14?

8 MR. SPORKIN: -- I'm saying which, where should it
9 come from? I'm not suggesting it.

10 MR. SILVER: I've got to tell you a story. Stanley
11 has never been able to lead me when I knew it.

12 The third or fourth day Stanley was at the
13 Commission he was heard going down the hall yelling he'd
14 uncovered the greatest fraud in the history of the Commission
15 and that an enforcement action and probably a criminal
16 reference should be made immediately. And I wondered how a
17 guy who was hired to study extensions of credit had, well, he
18 discovered this tremendous sin of a mutual fund that had
19 decided to sell its shares on credit cards.

20 Well, of course I thought this was pretty
21 innovative myself. But of course it technically was a
22 violation. And I remember thinking that this strange guy in

1 the green eyeshade would never go anywhere. That was 1962,
2 Stanley, '61?

3 MR. SPORKIN: Oh boy.

4 MR. SILVER: A question of where regulation should
5 come from.

6 MR. SPORKIN: Now where should this regulation and
7 enforcement generate? Should it --

8 MR. SILVER: Well, let me --

9 MR. POLLACK: What do you think? Answer your own
10 question.

11 MR. SPORKIN: What do I think?

12 MR. POLLACK: Yeah.

13 MR. SILVER: He asked me the question, Irv.

14 MR. SPORKIN: You go ahead.

15 MR. SILVER: I think it's really a two-way street.

16 And I think too little time has been spent on the issue I
17 tried to raise before that while an enforcement program, Irv,
18 I think can straighten people or a profession out for a while,
19 unless it carries over to a regulatory program its effects are
20 likely to be transitory. And I think in the history of the
21 Commission in looking at a lot of the cases I think that the
22 Commission has lacked a mechanism for distilling from

1 enforcement cases the lessons for regulations.

2 I will give you a few quick examples: The Tino
3 DeAngelis Salad Oil case which in its day was a big, big case,
4 big fraud, 1965. That case involved and brought down into
5 bankruptcy the sixth largest firm on the New York Stock
6 Exchange, Ira Haupt and Company. The whole gimmick here was
7 speculation in future contracts on soybean oil.

8 And the case was resolved. It was a very colorful
9 case. Tino DeAngelis went to jail. Ira Haupt creditors were
10 paid off by the New York Stock Exchange. However, only six or
11 seven years later Al Sommer went over to the White House,
12 something he told me he regretted, but at the behest of the
13 Commission to tell the White House that the SEC had absolutely
14 no interest in the legislation that established the
15 Commodities Futures Trading Commission. Somehow it never
16 percolated back onto the Commission's agenda that futures
17 trading could lead to the bankruptcy of New York Stock
18 Exchange firms.

19 Georgia Pacific was treated as a big case. What
20 was neglected was that in Georgia Pacific, looking at this
21 from a regulatory standpoint, that in Georgia Pacific the
22 company was using its pension plan to manipulate its own

1 stock. Yet, at the same time the Commission manifested no
2 particular interest in the congressional hearings that led to
3 the enactment of ERISA.

4 So that the lessons to be drawn from these cases
5 and legions of others is that there has been no mechanism to
6 create an historical memory or distill the experience of
7 enforcement into a regulatory program.

8 MR. SONDE: Dave. Dave, I disagree. I think that,
9 I mean I think the essence of the program at its best was not
10 to bring cases that were just bad boy lessons that anyone
11 could separate him or herself from. I think the genius of
12 Stanley and Irv's program was that you went after the
13 institutions and you tried to prove to the institutions that
14 they couldn't simply say it was this one rotten apple in the
15 institution that somehow infected it and made it the job of
16 the institutions.

17 I have a very different view of the CFTC and the
18 ERISA than you do. I frankly think that we had such, and by
19 "we" I mean the enforcement staff, had such a reputation for
20 tenacity and integrity that the industry was afraid to leave
21 it in the hands of the Commission. And so they went off to
22 something that was supervised by the Agricultural Department

1 or the Department of Labor rather than to give that power to
2 the SEC.

3 And I think if you look at the institutional
4 reaction when we pushed at the accounting firms and we went
5 and brought cases after cases and we brought them against law
6 firms the industry, in this case the accounting industry and
7 the bar pushed back and pushed back in a political and
8 institutional way and said get off my back. And there were
9 responses at the elected level to those kinds of things so
10 that for a while it did happen. And it's only this year that
11 we actually see substantive regulation now for the first time.

12 MR. POLLACK: I think there's part truth to both of
13 your arguments. The principal reason that the Commission did
14 not want to take it on was that it viewed the futures business
15 as one dealing in pork bellies. We did not at that time
16 appreciate the growth that was going to take place in
17 securities futures and other financial instruments trading.

18 With respect to the pension funds I think they felt
19 that was adequately covered by ERISA. We had a view that we
20 had a tough time getting our appropriation. We had a small
21 staff. We felt that if we got into these other areas we would
22 not get the money that we needed or the personnel that we

1 needed to do an effective job. So you're right, David, that
2 they missed the big one.

3 But take McKesson & Robbins which showed that the
4 auditing profession missed completely, the physical taking of
5 inventory. Take Ward LaFrance investigation back in the early
6 days, that exposed the lack of power in the statute to take on
7 frauds in the purchase of securities. And that led to Milton
8 Freedman's suggestion to adopt a rule under Section 10(b) of
9 the Exchange Act covering both the purchase and sale of
10 securities.

11 My own understanding was there was a basic
12 reluctance to extend the legislative scope of our activities
13 into areas that we thought did not directly affect the
14 securities industry. We weren't that smart to be prescient
15 about how futures trading was going to grow or how people were
16 going to use pension funds for piggy banks.

17 I would think that was the principal reason for the
18 actions of the Commission at that time.

19 MR. SPORKIN: Irv, well obviously our whole purpose
20 was always to have a regulatory response. We did it with 15c-
21 211. We did it with Taeco. We'll get, we'll get into all
22 those. But it was never really to leave it in a few cases.

1 But my recollection, and you fellows tell me if I'm
2 correct, there was always a fear on the Commission about
3 taking enforcement action. They seemed to cringe when Irv or
4 I would come there with a new case, afraid what that would do
5 to the industry, to the markets and whatnot. And, therefore,
6 I think that was one of the reasons that you didn't have a lot
7 of the enforcement activity generated by the Commission.

8 Now, that's different than I think Corporation
9 Finance because, as you recall, Richard, there used to be the
10 word around the Commission was "the Division." There was no
11 other thing but "the Division." And you knew what "the
12 Division" meant. It didn't mean the Division of Enforcement.
13 It meant the Division of Corporation Finance.

14 MR. ROWE: There was no Division of Enforcement,
15 Stanley, so it couldn't have meant that.

16 MR. SPORKIN: Well, I mean but there were other
17 divisions. But it was "the Division" was the Division of
18 Corporation Finance. And that's what it seems to me is where
19 the Commission put its emphasis and resources. Am I right or
20 wrong on that?

21 MR. ROWE: Well, I think you're right, Stanley, for
22 a variety of reasons. The mutual fund industry at that time

1 was burgeoning but it hadn't anywhere near reached the level
2 it is at today.

3 MR. SPORKIN: You had Barney and Manny who were
4 division directors.

5 MR. ROWE: We had ex-division directors on the
6 Commission. But also that was the gateway to financing
7 companies. And you put a lot emphasis on that. It was the
8 first statute, it was the first statute, the '33 Act, which is
9 the disclosure statute. And so our enforcement program as
10 such was to enforce the principal regulatory statute we had
11 which was not really a regulatory statute, it's a disclosure
12 statute, but it was to put teeth into the disclosure.

13 But we didn't, we didn't need injunctive authority,
14 for example, because if you start a stop order proceeding the
15 offering can't go forward but you're not accomplishing
16 anything unless you bring a case and establish some kind of
17 standard through that case.

18 MR. POLLACK: You know, it's also the separation of
19 enforcement for example from regulatory that had the same
20 impact. Because we could in the one division immediately
21 after an enforcement case get the regulatory people to take on
22 a new rule or a new approach to the problem. So I think that

1 is also what caused you to think there were deficiencies.

2 MR. SPORKIN: And now you had --

3 MR. SILVER: Well also, Stanley, just to say it's
4 clear that in the '50s the Commission for general
5 philosophical reasons had abandoned regulation as an avenue
6 for the markets and in other areas. So that you had a turning
7 away. You never regulated the exchanges or the markets in the
8 '50s.

9 Second, as Dick implies, in the '50s certainly
10 there was a revival of commerce and industry after the war so
11 all of the action was on financing new companies. And then
12 you had the two towering figures of Manny and Barney even
13 before they were on the Commission who drew the Commission's
14 resources into this area.

15 MR. POLLACK: In those days the Commission
16 personally reviewed every registration statement.

17 MR. SILVER: Yeah, yeah.

18 MR. POLLACK: So they didn't have time to do
19 anything else.

20 MR. SILVER: It was then Irv and to a degree Ralph
21 Saul, two towering figures in their own, who if you want to
22 personalize the thing started to draw the Commission back into

1 other areas. But again as I say the whole thing time makes
2 the man or man makes the time?

3 MR. SPORKIN: Let me ask you fellows, Ted, let's
4 see if can, Tom, well, Ted, what was the most important
5 accomplishment that the division, your division had during
6 your time, the enforcement accomplishment?

7 MR. ALTMAN: I think it fits into what you were
8 just talking about. To spend a minute on the subject we just
9 finished, I think the reorganization of the Commission in the
10 '70s, when the current Enforcement Division was formed, was
11 intended in large part to get enforcement out of policy
12 making, to let policy making be done by regulators. It had
13 some political overtones to it. But just put enforcement in
14 the enforcement area and take it out of policy issues.

15 But what I observed was that enforcement cases
16 started leading the way for regulation. I mentioned
17 previously valuation of securities. The first matters that I
18 recall with the Commission paying any attention to valuation
19 of securities were enforcement cases. From those enforcement
20 cases came a series of releases from the Commission that
21 created a milieu in which investment companies, and from the
22 investment companies others who would be faced with valuation

1 problems would have a guideline to operate.

2 Similarly, enforcement cases led the way into
3 brokerage abuses. Ultimately that turned into abandonment of
4 the minimum rate structure at the New York Stock Exchange,
5 NASD rules trying to separate distribution of mutual funds
6 from use of brokerage commissions to pay for that. Now
7 there's been a pushback and an ebb and flow in it but what I
8 saw and what I saw get more effective with the creation of the
9 Division of Enforcement is focus on problems through
10 enforcement cases and a regulatory pushback.

11 Today there are notorious accounting and financial
12 reporting scandals. If there is going to be any kind of
13 effectiveness that comes out of the enforcement cases these
14 matters generate it's not going to be the cases themselves but
15 it's going to be the atmosphere and the procedures and the
16 attention to integrity they encourage and help build into the
17 reporting system.

18 There are regulatory initiatives coming out right
19 now that require an apparatus where personnel all the way down
20 the line and up to the top companies are accountable for how
21 they put financial and other information into their reports
22 and make it available to the public and how timely they do it.

1 Although it starts with enforcement, if it's going
2 to be effective, comes out in a regulatory program.

3 MR. SPORKIN: Tom, I guess I don't have to ask you
4 what was the most important case but why don't you tell us a
5 little about Texas Gulf Sulphur. That was your, you brought
6 that did you not? It was during your time?

7 MR. RAE: Well, it was generally Ed Jagermann and
8 Tim Callahan, two of the most famous cowboys in the
9 Commission's history, investigators who were from New York,
10 Washington, or wherever they'd choose to be. But there was
11 for the first time in New York -- or Washington at that time
12 we'd organized a market surveillance unit that watched unusual
13 aberrations in the marketplace from day to day. And a
14 gentleman named Peter Fried started to notice in Texas Gulf
15 Sulphur a number of aberrations in the trading, unusual
16 purchasing in that.

17 So we after investigation obviously this company
18 had made a sizeable discovery of ore. I believe it was in
19 Labrador as I recall.

20 MR. POLLACK: Canada.

21 MR. RAE: In Canada. And the insiders knowing when
22 that discovery was announced would have a profound effect on

1 the market value of the stock went out and bought a lot of
2 stock.

3 MR. POLLACK: Well, that case really also started
4 because the young woman who was watching the Dow Jones tape
5 noticed --

6 MR. RAE: Ingrid? Ingrid Novak. She worked for
7 Peter Fried, yeah.

8 MR. POLLACK: Yeah. She noticed that on one day
9 there was an announcement of the greatest mining discovery in
10 Canada in history. Ten days later there was a disclaimer.
11 And the reason the company did that is because it was trying
12 to go around and buy up the surrounding land.

13 And so, you're right, we sent Jagermann up to
14 Canada. And in two weeks' time he made probably one of the
15 most outstanding insider trading cases in the history of the
16 Commission. And then, of course, once we brought that case we
17 also turned to the regulatory side. That's when we asked for
18 disgorgement for one of the first times.

19 MR. RAE: Irv, if you recall though we went to the
20 Commission. We were opposed by the Office of the General
21 Counsel in Texas Gulf Sulphur because these were not face to
22 face transactions between these members of management and

1 members of the investing public, they were done on exchanges.

2 And we asked whether the Commission itself had authority to
3 bring this kind of case.

4 And if you could believe it, these issues were
5 argued for two to three days before --

6 MR. POLLACK: Chairman Cary had put that to rest in
7 the Cady, Roberts case.

8 MR. RAE: No. Came up again.

9 MR. SILVER: Cady, Roberts the argument at the
10 table, Tom and I were chatting about this, the decisive
11 meeting was a four hour Commission meeting with about a dozen
12 staff members taking a dozen different points of view, maybe
13 13 or 14 different points of view ranging all the way from do
14 nothing to release.

15 MR. RAE: I think Cady, Roberts more pressed on the
16 existence or non-existence of a prior fiduciary --

17 MR. SILVER: The street had been trying to
18 distinguish Cady, Roberts on the grounds it involved a broker,
19 a regulated person. And, therefore, the argument was that
20 people have fair warning that this might apply --

21 MR. RAE: There was no face to face transaction.

22 MR. SONDE: Part of the irony of Texas Gulf Sulphur

1 was after the case was brought it was actually tried by the
2 General Counsel's Office rather than what used to be the
3 enforcement staff. And ultimately I think a lot of the
4 effectiveness of the program was lost because the messages
5 didn't get back the way Ted Altman's describing them to the
6 regulators. And it ultimately dissipated what I thought
7 otherwise could have been a significant accomplishment.

8 MR. ALTMAN: What dissipated?

9 MR. SONDE: The notion, the notion that there could
10 be lessons learned by the same staff --

11 MR. ALTMAN: Right.

12 MR. SONDE: -- that could carry it back to the
13 mutual fund industry on valuation or otherwise because the
14 kids got caught up in the actual trial of the case and got
15 lost if they were still around to come back and --

16 MR. SPORKIN: Well, there's no more landmark cases
17 in the insider trading program than Texas Gulf Sulphur. I
18 mean that still is the keystone case. And I think, but I
19 think really the point was, and this happened in a number of
20 cases, Irv, if you recall, that you had more difficulty
21 getting the case through the Commission than you do getting it
22 through the courts.

1 MR. POLLACK: Well, but eventually my recollection
2 is that the Commission was the one that rejected a compromise
3 in that case and said go to court and sue them.

4 MR. SPORKIN: Right.

5 MR. POLLACK: And it may have been Commissioner
6 Owens if I remember correctly who was the strongest up there.
7 He wanted to put them in jail.

8 MR. SILVER: Yeah. Manny, Manny Cohen was home
9 recovering from his heart attack. Hugh Owens was in the
10 chair. And those of you who remember Hugh he wasn't a man of
11 many words. But he listened to these arguments go on for
12 hours about what to do. And I could notice he was getting red
13 in the face. And finally he burst out saying I think this
14 should be a criminal case. And that sort of decided the
15 issue.

16 MR. POLLACK: The problem, the big problem we had
17 incidentally was because this was a novel promotion of the law
18 as well as regulation, we had to go around the country
19 debating with people as to the value of insider trading cases.
20 Some economists said we were crazy, there's an efficient
21 market out there and you want these people to do the trading
22 so that there will be something in the market to indicate

1 there's information that hasn't been given to the market.

2 I thought that economic analysis had been put to
3 rest. But about two months ago I read another economist who
4 wrote the same thing.

5 One of the reasons enforcement is so important in
6 policy making is what Stanley said. The Commission may be
7 reluctant to go out and attack what looks to be established
8 principles in the establishment that are holier than God. And
9 so unless you get some enforcement activity that shows that
10 there is some skullduggery, there is some corruption there,
11 there is some abuse there, it sometimes is very difficult to
12 push a policy issue.

13 I think your Sarbanes legislation is probably the
14 most dramatic example I can give. If it hadn't been for your
15 Enron and your WorldCom and your Cendant cases there would
16 never have been that legislation. Indeed, it started off with
17 just the auditing legislation. But once you began to get the
18 other scandals there was no opposition anymore because the
19 lobbyists were destroyed in their ability to lobby and
20 Congress, the administration could not defend the existing
21 structure even with all the best economists in the world.
22 There was something wrong with the regulatory program that had

1 to be addressed. And so you get the pendulum swinging all the
2 other way.

3 And it shows you the importance of what disclosures
4 will do in creating the necessary environment to get your
5 programs enacted.

6 MR. SONDE: Irv, do you remember that one of the
7 things I remember about a lot of the Commission discussion was
8 the notion that these respectable accounting firms, these
9 respectable law firms, these respectable brokerage firms
10 wouldn't be a party to this fraudulent scheme. And how could
11 we even possibly suggest that these institutions would be
12 parties to this type of activity?

13 Fortunately that argument has disappeared a bit.
14 But in the current climate --

15 MR. POLLACK: But if you take the Carter Johnson
16 case the enforcement people were able to show that here was a
17 law firm that knew that this issuer was continually putting
18 out erroneous information and yet did nothing about it except
19 internally. They never tried to do anything other than --

20 MR. SONDE: But, Irv, you remember the debate. I
21 mean it was only settled by Stanley's efforts in the Sarbanes
22 legislation about what was the lawyer's duty when confronted

1 with fraudulent activity and how far did you have to go? And
2 the bar went bananas over whether or not a lawyer had a duty
3 to do anything.

4 MR. SPORKIN: Well, went so far as the Commission
5 or staff, General Counsel put out a letter that said they're
6 not going to use 2e to discipline lawyers anymore. And that
7 always bothered me. And by some hook or crooks the new
8 legislation has that rule is now part of the statute.

9 But we will let that go to the next discussion.

10 Now let me ask you this question here: what about,
11 you know, we always had a problem of, Irv, you and I were
12 always afraid that we were taking on one of the big boys or
13 the big girls, or the big boys I guess, that we were afraid
14 that we were going to be, they were going to run around us to
15 go up and talk to the Commission. Ex parte was a big problem
16 then.

17 What do you know about it? What was the --

18 MR. POLLACK: Well, what I know about it is I can
19 tell a quick story. You came to me one day --

20 MR. SPORKIN: Oh, Jeez.

21 MR. POLLACK: -- and said that somebody had gone
22 to the Commission or the chairman and had obtained their

1 understanding that we would remove a suspension of stock or
2 something like that.

3 MR. SPORKIN: Yeah.

4 MR. POLLACK: And they had a release that they had
5 typed up that they gave to you. And you said this is
6 terrible, what are we going to do about it?

7 I said where's the release? You said you threw it
8 in the basket. I said get it out of the basket, that's going
9 to be the first exhibit when we sue them. And that's what we
10 did and that's how we handled an ex parte communication to the
11 Commission.

12 MR. SPORKIN: What did you fellow do though? Did
13 you have, Richard, did you have problems with people going
14 around you, going to the Commission, speaking to Manny or
15 Barney? Well, they wouldn't talk to Barney, would they?
16 Barney was very --

17 MR. ROWE: Sure, there were efforts to do that. I
18 remember in National Student Marketing, Ted probably remembers
19 this too, that White and Case which was one of the law firms
20 that was sued in that case put a tremendous amount of pressure
21 on the Commission or attempted to. The Commission did not
22 cave to the pressure.

1 MR. SPORKIN: Was there any rules against it? Did
2 we have any rules then?

3 MR. SONDE: Yeah, you had the same rule that you
4 have today basically. But I don't think anybody paid
5 attention.

6 MR. SPORKIN: What is the one we have today?

7 MR. ROWE: Well, I think the Commissioners had to
8 put something in the file that there was an ex parte
9 communication.

10 MR. SONDE: But the real concern, Stanley, I
11 thought was more on a political level. I mean we had heard
12 shortly after White and Case was sued in the National Student
13 Marketing case that the Commission, that is the staff who were
14 trying the case, that the Commission was about to withdraw or
15 amend the complaint. And we understood that to be an
16 institutional concern.

17 But I think the more serious one frankly was the
18 political pressure. I mean I remember when I was still in the
19 General Counsel's Office and Murray Chotiner showed up in my
20 office one day -- those of you that don't remember, Chotiner
21 used to be part of the Republican establishment in an earlier
22 day and era -- and he told me that the chairman had just

1 instructed the staff as to how to settle the case. And I said
2 I don't get my instructions that way.

3 And the next thing we knew we picked up the phone
4 and we had a grand jury in New York. And if Chotiner hadn't
5 died he probably would have been indicted.

6 MR. SILVER: Well, the political thing of course
7 went all the way back to the time of the Re and Re
8 investigation and the AMEX. Congressman McCormack, I think
9 then Democratic leader in the House, later Speaker of the
10 House, called Ralph Saul and just point blank directed him to
11 drop the investigation. Ralph didn't and the rest is history.

12 But these things go all the way, all the way back.

13 MR. POLLACK: His assistant was indicted in that.

14 MR. SPORKIN: Well, you had the Goldfine case
15 there, what was that all about?

16 MR. POLLACK: Well, that was Sherman Adams and the
17 White House and their attempt to interfere in a case against
18 Goldfine based on a failure of his company to file its reports
19 for numerous years. And the then General Counsel I think, or
20 he was associate --

21 MR. SPORKIN: Was it Meeker?

22 MR. POLLACK: Meeker.

1 MR. SPORKIN: Yeah.

2 MR. POLLACK: Had been called to the White House
3 and had some meeting over there that he never told us about.
4 But the result was Mr. Goldfine's indictment.

5 I think all of this illustrates that the staff had
6 a impeccable reputation that it was a mistake for anybody to
7 try to use either political or congressional pressure because
8 it would merely get them into worse trouble.

9 Indeed, I remember a former U.S. Attorney in New
10 York asked the Corporation Finance Division for a one week
11 delay in some stop order case, as I recall. And the question
12 was should we give it to him because he went through some
13 congressman rather than asking for it directly. And so the
14 way we resolved that is they were entitled to the one week
15 extension, it didn't mean anything. But I called him up and
16 said the next time you do this you're not only not going to
17 get an extension you're going to be subject to an
18 investigation.

19 And he said, Gee, Irv, I'm sorry. Somebody told me
20 that was what I should do. I should have been smart enough
21 not to do it.

22 And I found in the time of my career that

1 congressmen or their staff if they would call up and you would
2 just say you should tell your congressman that this is
3 something that he ought not to be interested in that would end
4 it. And when it didn't then it would normally lead to
5 something worse. And so the result was, for example, the
6 Speaker's assistant gets indicted for attempting to influence
7 some matter.

8 I think that's the core. If you're going to run an
9 enforcement program of any respectability, the people out
10 there, whether it's the politician or whether it's the
11 lobbyist or whether it's the law firms or the accountants,
12 they have to know that influence will not affect how cases are
13 handled. And I think we made a major effort to do that.
14 Indeed, when there was any corruption on the part of our staff
15 that became a priority for us and they wound up being indicted
16 and convicted in the very limited number of cases which we
17 had.

18 MR. SPORKIN: You know, let me ask you this, we're
19 talking about staff, Commission, but there are human beings
20 here. Ted, in your division you had a number of interesting
21 people. Just describe who these people were and what they
22 did. You had Sid Mendelson working in your division. You had

1 Sid Mendelson and a number of others. What were the
2 characters, what were they like these characters?

3 MR. ALTMAN: When I came there Sid Mendelson was
4 what was then called the chief enforcement attorney for the
5 Division of Corporate Regulation. He was responsible for all
6 investment companies, investment advisor regulation. I'm not
7 sure people in trading and markets would agree that he was
8 responsible for investment advisor enforcement but there was a
9 little turf battle that went on there.

10 He --

11 MR. SPORKIN: Sol Friedman you had.

12 MR. ALTMAN: Sol was the head of the division. He
13 would hold meetings. And the division would function. I
14 wasn't high enough at the time to really understand what Sol
15 was doing.

16 MR. SPORKIN: Yeah.

17 MR. ALTMAN: I'm not sure even the guys who were
18 real high understood what Sol was doing. But the division
19 ran. I think it, well, from what I could see it was
20 effective.

21 MR. SPORKIN: Tom, your area?

22 MR. RAE: We had wonderful, wonderful people. We

1 had Art Matthews and Chick Marku and, you know, we had a great
2 staff, tough roster.

3 MR. SPORKIN: Later you had Eddie Jagermann. Go
4 ahead, tell us about it.

5 MR. RAE: I was going to talk about ex parte
6 communications.

7 MR. SPORKIN: Go right ahead.

8 MR. RAE: Because you were the worst one I
9 experienced at the Commission.

10 Irv and I, I was associate director and Irv was
11 director, we were going to name an assistant director. You
12 very much wanted that job and I'd made it clear you were
13 certainly the favored son. But I said I shouldn't talk to you
14 because I'm not talking with the other people being
15 considered. And Stanley said okay.

16 The next morning about 9:00 o'clock he opens my
17 door and he said, by the way, Judy had a baby last night and
18 we named it Thomas Sporkin.

19 (Laughter.)

20 He wanted anything for that.

21 MR. SPORKIN: Oh, my God. Oh, my God.

22 MR. RAE: It's true.

1 MR. SPORKIN: All right. All right. That's not ex
2 parte that's bribery. What do you mean?

3 (Laughter.)

4 MR. SILVER: Stanley, Tom referred to Eddie before
5 as I remember you were cowboys. The notes I made referred to
6 him and Tim Callahan as knights errant of enforcement. They
7 roamed the country righting wrongs wherever they would see it.
8 Others called them loose cannons. So it depends on your
9 point of view.

10 The interesting thing is that Tim told me that his
11 background, I'm not sure where Eddie came from, but Tim had
12 come over to the Commission at the end of prohibition and that
13 he said that a lot of the early enforcement people,
14 investigators at the Commission came from the agencies of
15 government that chased rum runners around. And that does
16 remind me of some of the attitudes of some of the early
17 regional administrators who would raid the offices of
18 broker/dealers and give them 24 hours to get out of town,
19 which meant they were simply going to go to some other region.
20 But that was typical for the time.

21 MR. SPORKIN: Let me ask you, well, Eddie Jagermann
22 couldn't exist in today's environment. There's no such as a -

1 - Eddie Jagermann what I used to love, what Irv did to me one
2 day he calls me in he says, Stan. Yeah? He says, from now on
3 you're going to supervise Eddie Jagermann. And I said, Well,
4 Irv, what happened when you were supervising Eddie Jagermann?
5 Well, he didn't answer that.

6 But in any event Stanley starts to do that to me
7 when I went down to the division. I won't put names on the
8 table but there were a number of people used to say I should
9 have supervised, and I couldn't supervise.

10 Now, but they told me this, can you imagine
11 supervising Eddie Jagermann now? Could you imagine? Nobody
12 could supervise. Eddie Jagermann, the story you tell, Irv, is
13 that one day he had a call from the immigration people they
14 were holding somebody in custody who claims his name is Eddie
15 Jagermann and he works for the SEC. He had gone down to
16 Brazil to bring back some of these ex-patriates who had -- it
17 was Eddie Gilbert and Burrel, Lowell Burrel, and he was going
18 to go and bring them back himself. But this, I mean this
19 fellow was so bigger than life that you would not, you would
20 absolutely not believe him.

21 Got a call one day from him and, Yeah. I said,
22 Eddie, what's up? And he had the biggest broker here in town

1 he says. Stan, he says, I got a Section 5 case against, what
2 was it, I forget who the biggest broker was in town, but it
3 was awful, I don't think it's any longer in existence, but in
4 any event Sharon K. Ritchie was its compliance officer, used
5 to be with the Commission. In any event he says I got the
6 Section 5. I said Section 5 against that firm? That's
7 impossible. They're a good firm. No.

8 He says, no, I got it. He says go to the
9 Commission now and get authority and bring the case.

10 I said, Ed, -- you know, talk about Harvey Pitt
11 wants real time enforcement, this was real time enforcement --
12 I said, Ed, tell me what do you have? He says, Well, I got a
13 confession. I said, What do you mean you got a confession?
14 And he puts on Sharon K. Ritchie who confesses that they
15 violated Section 5. Not only did they violate but they were
16 going to -- they consented to an injunction on the phone.
17 And I didn't know what the hell to do with it.

18 I mean I never had anything like this. And of
19 course I wrote it down, took it to the Commission. We filed a
20 case and he made it that way. This is the way this guy
21 operated. The other thing he did which I thought was
22 marvelous is I was in interrogation with him. And he starts

1 out with this witness and he says to him -- I think you
2 remember this, Irv -- he says, Now, on such and such a day you
3 did so and so. On this day you did that. On such a day you
4 sold the stock. On such and such a day you paid that guy off.

5 And the guy, the witness turns to his lawyer. He
6 says, They've tapped my lines. He was certain that there was
7 wiretapping going on because Jagermann after two questions
8 could know the exact scheme that was taking place and he knew
9 exactly what was happening and he would tell the guy exactly
10 what the person did. And to this day I remember him telling,
11 the guy turning to his lawyer says they violated the law,
12 they're engaged in the wiretapping. And that was the amazing
13 kind of person.

14 But those are the kinds of people we have.

15 Now, we've got a few minutes left. And I want to
16 ask each of you because I think this is very important, what's
17 the legacy, what can we learn from your days at the
18 Commission, each of you, that can help the Commission today in
19 carrying out its program?

20 Ted, you want to start and we'll get Tom and then
21 we'll.

22 MR. ALTMAN: I think overall if you can create an

1 atmosphere of integrity and you could run it through each of
2 your specific enforcement and regulatory programs it overrides
3 the specific program. The atmosphere is much more important
4 than the mechanics.

5 MR. SPORKIN: Tom, what do you think?

6 MR. RAE: I agree with what Ted had said. I think
7 morale, esprit de corps is very important. And this agency
8 has gotten a lot of criticism lately in some areas because
9 where were they when all these things happened? I think you
10 can't let criticism stop you. You do your best job, you've
11 got a charter now and do it. But I think just the
12 determination that we had in the early '60s, we were going to
13 move things around and change things and we did it.

14 MR. SPORKIN: Tom, in your day you and Irv when you
15 ran the division, and I must tell you it was the best run
16 division I've ever been affiliated with, the blend was so
17 terrific between the two of you, but what you also did which I
18 think is important is you established a meritocracy in the
19 division that people got ahead based upon their work effort.
20 Is that important?

21 MR. RAE: Yeah.

22 MR. SPORKIN: How did you do that?

1 MR. RAE: We were awfully lucky. Like we hired a
2 gentleman named Art Matthews once who was one of the most
3 brilliant securities attorneys I've ever met, became
4 nationally prominent. He came in, he'd been in a bridge
5 accident, had a six weeks growth and had a metal sticking
6 through his cheeks. He looked like hell. But during the
7 interview there was something unique about that individual.
8 He's the only guy I know that used to read advance sheets in
9 the cab like Irv does. Nathan Frankow. We just had so many
10 bright people.

11 But you're right, didn't make any difference who
12 you were, your school didn't mean -- I'm University of
13 Wyoming. Generally I couldn't get an interview at Wall Street
14 if I tried. But I think I succeeded at the Commission because
15 they didn't care where I went to law school. It depended on
16 the work I did and the dedication.

17 MR. SPORKIN: Ted, what do you think? What's the
18 legacy, what is it from your work they can learn?

19 MR. SONDE: Well, I think I agree with what Ted
20 said and also what Tom said. I mean I think of Art Matthews
21 went to Albany Law School. Dave Ferber went to Albany Law
22 School. It was a meritocracy. And I think the greatest thing

1 that we gave to the agency --

2 MR. SPORKIN: Or the Chairman. The Chairman went
3 to --

4 MR. SONDE: The Chairman went to -- I mean Harvey
5 used, when Harvey was fresh out of law school, he went to St.
6 John's. And for years he used to be ashamed of that. He used
7 to feel like he couldn't compete. It was never ashamed of it
8 in an active sense, he was proud of it but he was always
9 treated like he was a second class citizen because he hadn't
10 gone to the right law school.

11 I think that the real lessons are the morale and
12 professionalism of the staff, the merits that Tom describes of
13 people rising on merit based on, frankly, their integrity and
14 their courage and their ability to do things. And, frankly, I
15 think we have to push back on the profession, the professional
16 firms, the accounting firms, the law firms, I think the
17 institutions that, you know, we're reading about and shocked
18 that we're reading about this. And for those of us who have
19 been there we're not shocked by it except that it keeps
20 happening again and again.

21 MR. ROWE: I think I'd echo everything that's been
22 said here. It's really the staff and their courage and

1 integrity. And I think they have to stand up and sometimes
2 it's tremendous pressure.

3 I remember, going back to National Student
4 Marketing Ted and I were talking earlier that the young lawyer
5 that was in charge of investigating that case came to me one
6 day and he said the lawyers knew everything that was going on,
7 what am I going to do? I said you're going to continue to
8 investigate the case and then you report back with your
9 recommendation.

10 And he did it. And we took the case to Ted and we
11 took the case to the Commission and we stood up to two major
12 law firms and a major accounting firm and one of the biggest
13 crooks that I ever ran into. But that's a different story.

14 MR. SPORKIN: David?

15 MR. SILVER: I would agree with everything that's
16 said but come back to the slightly earlier theme that I tried
17 to develop and that is the Commission must properly integrate
18 all of the information at its disposal and particularly
19 through enforcement into its regulatory program. There were
20 two brief shining moments when this tried to happen or the
21 attempt was made, one when the Special Study recommended the
22 creation of an office of program planning under Walter Werner.

1 And the second was when Irv was division director sitting on
2 top of regulation and enforcement.

3 The Division of Enforcement from the trading
4 division essentially gave rise to a great, great enforcement
5 effort. But I don't think the Commission has ever properly
6 utilized the enforcement results into their regulatory
7 program.

8 MR. SPORKIN: What happened to the Walter Werner
9 group?

10 MR. SILVER: Walter Werner group came a cropper
11 because Walter was not -- wonderful man but was not capable of
12 winning any bureaucratic struggles within the Commission
13 because he was perceived by the operating division directors
14 to be treading on their toes. And also his energies became
15 dissipated when the Commission kept on assigning the problems
16 du jour to his group rather than the function they were
17 supposed to take part in.

18 MR. SPORKIN: Irv, what do you say?

19 MR. POLLACK: Well, I agree with the comments made.

20 I think that speaking from an enforcement point of view you
21 should be aggressive, of course have absolutely impeccability
22 and integrity but also be fair and reasonable in what you do.

1 And your programs should focus on those people who give
2 access to the market. I notice today they're called
3 gatekeepers.

4 The Commission cannot alone do the job. It must
5 instill in the people it regulates out there, and in its self-
6 regulatory organizations, an understanding that good
7 regulation is good for business and that people who engage in
8 self compliance and self discipline will get a benefit from
9 that not only in the quality of their business but in the
10 reaction of the Commission toward the issues and problems that
11 arise in any large organization.

12 I think the most important thing was the fact that
13 we sued, Stanley, probably every firm out there of size. And
14 yet after we sued them, we had their respect so that they
15 would call in advance and advise us whether they had a
16 perception problem or an actual problem and we would then
17 adjust whatever our remedies were to help them engage in
18 getting compliance from all their people within their
19 operations.

20 And with the growth that's taken place since the
21 years that we were responsible, it's even more important.
22 This agency with its limited resources, even with the great

1 increase it may get now under the Sarbanes legislation, cannot
2 do it alone. It must depend on those people out there to
3 create the culture that should emanate from the leaders of
4 your companies, the leaders of the capital markets in
5 recognizing that they have a responsibility to investors and
6 to society to do the job correctly.

7 MR. SPORKIN: Well, folks, that's the end of the
8 first panel. At exactly 3:30 we're going to start. This is
9 the warmup. Now we're going to go to the main bout at 3:30.
10 We'll bring in the heavyweights now.

11 (Whereupon, at 3:20 Panel One recessed to reconvene
12 at 3:30 for Panel Two.)

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14 \\

1 PANEL TWO

2 (3:30 p.m.)

3 MR. SPORKIN: These are all I guess ex-enforcement
4 people except Alan Rosenblat. He was left over from the other
5 panel and he's here now to join us.

6 Well, let us, what we have here is we've got Ted
7 Levine and, Ted?

8 MR. LEVINE: Let me suggest why don't we start by
9 people making any comments that they would like to make in
10 light of the first panel's discussion where they either agree
11 or disagree or have some comments that they'd like to make.

12 MR. SPORKIN: That's a good idea.

13 MR. LEVINE: And let's start with Wally Timmeny.

14 MR. SPORKIN: And, Wally, why don't you introduce
15 yourself so the audience can know who they're talking about.
16 Wally Timmeny was a former Deputy Director of the Division of
17 Enforcement.

18 Alan Rosenblat was with the Division of Investment
19 Management.

20 Ted Sonde was in every division in the Commission,
21 too many to name.

22 Dave Doherty was also the Associate Director of

1 Enforcement.

2 Ben Greenspoon was the head of the trial unit and I
3 guess associate director.

4 And Ted Levine was an Associate Director of
5 Enforcement during the relevant period.

6 And, of course, Irv was the first Director.

7 But go ahead, Wally. I'm sorry, I just wanted to
8 make sure that everybody knows who's here.

9 MR. TIMMENY: What I wanted to do by way of
10 providing a bridge between this panel and the first panel was
11 to go back to a point that wa being made about the formation
12 of the Enforcement Division.

13 There was a lot of discussion on the first panel
14 about Chairman Cary wanting to have an enforcement program in
15 the Division of Trading and Markets or the Division of Trading
16 and Exchanges. And that was all very true.

17 But the Division of Enforcement was founded if you
18 will by Chairman Casey. And Chairman Casey's goal in creating
19 the Division of Enforcement was from my perspective to remove
20 Irv Pollack from the regulatory function in the Division of
21 Trading and Markets. One of, you know, history is a matter of
22 perspective but I was a young kid down in the Division of

1 Investment Management working on a project that Jack Dudley
2 had assigned. He sent us out to do an examination of a fund
3 complex. He was really interested in turnover, the amount of
4 portfolio turnover in the fund. And he sent a guy named Dan
5 Schatz and yours truly out there to look into turnover.

6 And as we were looking into turnover we stumbled
7 onto something called a give-up basically. It was a matter of
8 the fund assigning its brokerage to a certain broker/dealer
9 who in turn would split a part of that brokerage with another
10 broker/dealer and the second broker/dealer would sort of take
11 instructions from the fund manager as to where to send the
12 money. All of this demonstrating that fixed rates were a
13 farce, that there was a lot of slush in the commission
14 structure. And the money managers and whatnot were taking
15 advantage of it.

16 When we came back with this information about how
17 we had discovered these give-ups going around to a whole
18 string of firms and ending up in a firm called Dishe Easton in
19 New York we brought that up to Irv and made a point about how
20 the give-ups were working, he took that and I think it was
21 very much the formation for what he did in the fixed rate
22 hearings. And he really worked hard on that and toppled the

1 whole fixed rate structure in essence.

2 And as part of that effort when he was undertaking
3 that effort I think it was Chairman Casey's view that there
4 was too much of an enforcement flavor in this regulatory
5 process and that someone else other than Irv Pollack ought to
6 be setting the regulatory tone with respect to these very
7 important market issues.

8 And that's how from my perspective the Enforcement
9 Division was formed. It was formed not to create a wonderful,
10 effective enforcement unit, rather it was the law of
11 unintended consequences in the sense that Irv was pulled out
12 of regulatory stuff and put in charge of enforcement in the
13 hope that he'd no longer be involved in the regulatory side.
14 In fact he was in any event, but even more so I think because
15 of the cases that we brought and the way we used the cases to
16 set regulatory policy.

17 MR. SPORKIN: But Wally, I'm not quarreling with
18 what may have been an objective but I do think historically
19 what happened was the Wells Commission that was set up to look
20 at enforcement. And I think that was a recommendation that
21 came out of the Wells Committee.

22 MR. SONDE: Wells came out of the National Student

1 Marketing case because they were offended that we had sued
2 them without giving them notice.

3 MR. SPORKIN: Yeah, I know but I think that one of
4 the recommendations out of it was to set up the Enforcement
5 Division, as it was also to give Wells submissions.

6 MR. SONDE: My perception is the same as Wally's.
7 And Frank --

8 MR. SPORKIN: Well, what do you think, Irv?

9 MR. POLLACK: I can tell you what Casey said.

10 MR. SPORKIN: Yeah.

11 MR. POLLACK: And it's in the report that Dan Hawke
12 put together.

13 MR. SPORKIN: Right.

14 MR. POLLACK: On his last few days of leaving the
15 Commission I had a conversation with him. And we had an
16 excellent relationship the two of us and respected each other
17 and he was very candid. And he said, you know, I worried that
18 when I left the Commission you would undo the regulatory
19 policies that I thought ought to exist.

20 And I said to him, Well, I understand that, Bill,
21 but you're not going to be able to stop it.

22 And he then said to me, I now think you're right

1 but there's no way I can undo the program that we set in
2 place.

3 MR. SPORKIN: Right.

4 MR. POLLACK: So that there's no question that he
5 felt that he wanted some other person in the regulatory side.

6 MR. SPORKIN: All I was saying was I think the
7 division, the concept of the division came out of the Wells
8 Committee.

9 MR. POLLACK: It may have.

10 MR. SPORKIN: Does anybody else?

11 MR. POLLACK: There's always a number of reasons
12 why people will do things.

13 MR. SPORKIN: What was it? What was it, Ted?

14 MR. LEVINE: You're right. It was one of the
15 recommendations of the committee.

16 MR. SPORKIN: Yeah.

17 MR. LEVINE: But that's okay because --

18 MR. SPORKIN: Who was on the committee? It was
19 Demmler, Wells.

20 MR. LEVINE: Wells, Demmler and Manny Cohen.

21 MR. SPORKIN: Yeah.

22 MR. LEVINE: But the committee was at the behest of

1 the Chairman so what did you expect?

2 MR. SPORKIN: Well, I think --

3 MR. POLLACK: Let's move on though because I think
4 that's pretty much the most we can do in that area.

5 MR. LEVINE: Irv, with respect, I have a slightly
6 different perspective and in transition maybe into the later
7 years. And I was at the Commission from in '69 to '83 which
8 would cover this entire period. And two things that struck me
9 as I thought about this program. One is, and I mentioned this
10 at lunch, there were three distinct periods I will call the
11 golden years which I would say was like '70 to '77, then a
12 transitional period which was really Harold Williams'
13 chairmanship, and then there was like a return to deregulation
14 when John Shad came in.

15 And two things that I think were really important
16 in that context. One, in the golden years up to when Powell
17 became on the Supreme Court we had an incredible favorable
18 Supreme Court relative to the SEC. Both the 2nd Circuit, you
19 know Timbers was the former general counsel, you had a -- it
20 was a very well received agency. You got whatever you wanted.

21 It was the most expansive view of the securities laws. And
22 that made life easier.

1 You contrast the Capital Gains where injunction was
2 a mild prophylactic to Enron when it was a drastic remedy and
3 it would reflect the attitudinal change which impacted the
4 enforcement program.

5 Second of all, the period you just talked about the
6 enforcement program was not well known on Main Street. It was
7 an unknown program of a small agency. But once the Foreign
8 Payment program set in and it put it on the face of the map it
9 changed the attitude of everyone about enforcement. It became
10 more difficult because it became a more intrusive program than
11 it had been which was essentially a regulatory program.

12 And lastly, and people can disagree with this, it
13 was a simple program with no remedies except for the use of
14 creative relief in the early '70s. And once we started
15 overlaying both a more punitive program which happened when
16 Shad came in and more drastic remedies the courts became a lot
17 less receptive to the agency's mission as one of protecting
18 the public. It became much more difficult.

19 So we had all these debates about preponderance of
20 evidence against clear and convincing. All the debates of
21 whether you send an injunction or not. We flipped to the
22 administrative remedies.

1 And what I noticed in looking at this no implied
2 right of action the courts changed their view of us in a
3 manner which I think hurt the program but made it more
4 challenging and more creative. And so I think the program,
5 and I'll finish on this thing, a remedial program which was
6 the one that Irv talked about in the earlier panel, and
7 Stanley, where you try to accomplish and move industry
8 standards was a lot easier in both the court's and the public
9 eye to sell than a more punitive program which, by the way, I
10 think the public perceives the current enforcement program as.

11 And I think that happens to be today something that people
12 like but I think is a more difficult program to run in the
13 long run if it's perceived to be punitive rather than
14 remedial.

15 MR. SPORKIN: Let me, well, in line with what you
16 people are talking about the word that Irv and I came up with
17 we almost had a bipolar concept here, there were highs and
18 lows. Is that, David, is that your view of it? Wally, David,
19 is that your -- do you remember the highs and the lows?

20 MR. DOHERTY: I remember the highs. I don't
21 remember any really significant lows. I think that in any
22 aggressive enforcement program where you're out there on the

1 cutting edge you're going to get knocked down every now and
2 then and not have a good reception with the courts. But I
3 think overall the program really had a good rising impact to
4 it.

5 MR. SPORKIN: How about you, Wally, do you remember
6 the highs and the lows?

7 MR. TIMMENY: I'm hard pressed to think of lows.

8 MR. SPORKIN: Well, I have one here when they
9 turned off the spigot on going after lawyers. I don't know if
10 you remember, was that, you were here then or?

11 MR. TIMMENY: Yes. Yes. And I also, I also
12 recall. But we had what I would call budget difficulties, you
13 know, toward the end there, late '70s. There was really an
14 effort to cut back on the budget and so forth.

15 MR. SPORKIN: Right.

16 MR. TIMMENY: And there was a period when it was
17 not low, it was sort of funny when I think back on it. When
18 in the early it was 1970 or so when Judge Budge was the
19 chairman and he decreed that we would not take transcripts of
20 testimony, that we would go out with a yellow pad and
21 interview the witnesses. As a matter of fact, we wouldn't
22 even go from the home office, we should call somebody in the

1 regional office who would do the interview but make sure that
2 person used a yellow pad and not a transcript because --

3 MR. DOHERTY: And there actually were some
4 restrictions on making long distance telephone calls as well.

5 MR. TIMMENY: But I didn't, I never took that -- I
6 don't think that stopped us. I mean as a matter of fact we
7 worked around it. And actually we took that with a sense of
8 humor.

9 MR. SPORKIN: But don't you remember, don't you
10 remember we had a quota system that for every, every major
11 firm we hit -- I mean every minor firm we had to bring a case
12 against a major firm?

13 MR. TIMMENY: Well, no, that, that was a big --

14 MR. SPORKIN: You don't remember that? Don't you
15 remember that, Irv? Yeah, you guys remember that. That's
16 telling tales out of school. But go ahead.

17 MR. TIMMENY: But that was the big, I think a big
18 if I can call it transition because when the enforcement
19 programs were in the various divisions they did bring cases.
20 But they weren't really tackling the giants in any one
21 industry. When we put the enforce -- when the enforcement
22 program was all put together in one division I think the

1 hallmark of the enforcement program at that point was that we
2 would tackle anything. And that's when we brought the case,
3 we brought the Lockheeds, the Exxons, the Northrups.

4 MR. SPORKIN: Right. Right.

5 MR. TIMMENY: Every case was a big case.

6 MR. SPORKIN: Right.

7 MR. TIMMENY: And there was no hesitation to bring
8 it.

9 MR. SPORKIN: Right.

10 MR. TIMMENY: You know, we'd sit with Stanley at
11 the Commission for days on end arguing about the cases. And
12 Stanley had this I would call an iron behind because he would
13 sit in that chair for hours and hours and hours and argue with
14 the Commission as to why we should bring the case.

15 But there was never any hesitation to tackle the
16 major, the big cases. And that was different from before.

17 MR. DOHERTY: And I think that one of the big
18 differences as the home office enforcement program kicked into
19 gear was that we in effect had the equivalent of a reserve
20 squad. Unlike the regional offices who had to handle all the
21 matters in their region and were always stretched thin we had
22 the luxury of looking for problems that were arising.

1 And what we would try to do is tackle it in a
2 programmatic way and instead of just reacting to each matter
3 that came up on its own as we saw problems arising, we would
4 try to get out ahead of it, we would throw a lot of resources
5 onto it with the objective of getting at it quickly, getting
6 ahead of it, bringing a series of enforcement actions that we
7 would then hope would have a significant impact on the
8 violative conduct. And oftentimes we had a proposed
9 legislative objective as well if we made the right factual
10 record.

11 MR. SPORKIN: Now, do you recall, folks -- I'm
12 sorry, Ted, did you want to say something?

13 MR. SONDE: Well, I thought Dave really hit the
14 nail on the head because I remember when I first came from
15 General Counsel's Office to Enforcement which was in '74 and I
16 heard you, Stanley, talk about programs.

17 MR. SPORKIN: Right.

18 MR. SONDE: And that was a new word to me. I mean
19 I understood the word but I hadn't heard of it in the years
20 I'd been at the Commission before. And all of a sudden I
21 began to see that someone was looking at the big picture and
22 talking about how do we go after this area and that area. And

1 you created a series of programs. And, frankly, I was very
2 skeptical at the beginning because I didn't quite see how that
3 was evolving.

4 And it was that kind of input that I think really
5 created it. And I think, I mean it's exactly what Dave
6 described. And that was the process.

7 MR. LEVINE: Actually, I would want to, I think the
8 difference between the enforcement program then and the more
9 recent ones was we didn't announce programs like are done now.
10 We clustered a number of cases and then the program
11 developed, for example, insider trading.

12 Today or in the recent past people announce we're
13 now looking at corporations or we're now looking at
14 broker/dealers. And I think that's a big difference in the
15 way that, and also the difference is the program in the '70s
16 was multi-faceted, you did not know, it wasn't geared to a
17 program. Everyone thought that they were under investigation
18 for everything at every time. And that made everyone more
19 compliant.

20 MR. SONDE: But I always thought Shad came up with
21 the idea of insider trading as a way to divert us from other
22 things and then stumbled onto the Boeskys and the Mike

1 Millkens and the others. And I always thought that that was
2 an attempt to get away from Stanley's notion of program.

3 MR. SPORKIN: The other thing that they did, as you
4 recall, what we'll hear, because Ben was in both our division
5 and General Counsel, but did you fellows feel like I felt, and
6 Irv, I guess you were on the Commission at the time, that
7 there was an attempt to stifle the division in the sense that
8 -- and they did it in certain ways, for example they brought
9 in the General Counsel Reviewing Group? And what was that all
10 about, Ben? Did you turn traitor when you went up to the
11 Office of General Counsel?

12 MR. GREENSPOON: Of course. I knew who was paying
13 my salary.

14 (Laughter.)

15 MR. ROSENBLAT: I remember that very well. Harvey
16 instituted a program of reviewing every matter that went to
17 the Commission, not just enforcement actions --

18 MR. SPORKIN: Right.

19 MR. ROSENBLAT: -- but regulatory recommendations
20 as well, rule proposals. And we assigned, we assigned each
21 memo to a member of the staff. And then the supervisors would
22 all gather on Monday morning and we would go over each matter.

1 Now, I must say that we occasionally had some
2 problems with some of the enforcement matters. But in the
3 main the vast majority of the Division of Enforcement's
4 recommendations had no opposition from the General Counsel's
5 Office. The only thing that sometimes bothered me having come
6 from the Division of Investment Management it sometimes
7 bothered me that if there was something egregious but also an
8 Investment Company Act violation the tendency was, oh, let's
9 not confuse people. That's too hard. It's too technical.
10 Why don't we just drop that?

11 And very often that was done. And probably was a
12 good idea.

13 MR. GREENSPOON: Stanley, I would like to -- I did
14 not participate in that because at the time that Harvey was
15 the General Counsel I was working for you. But I would like
16 to say something a propos of some of my observations briefly
17 at the time I came to the Commission because you hired me
18 specifically to be in the trial unit. And the impression that
19 I got at that time was that you were going to, you wanted to,
20 you were going to beef this thing up because you were going to
21 do a lot of trial work and that you were going to go after
22 people who might think that the Commission was a toothless

1 tiger that did a lot of talking but when it came to having the
2 chips on the table they were gone. And so you were going to
3 create this trial unit.

4 And I'm happy to say, I'm happy to be a part of it,
5 frankly. And I think that in terms of contributions to
6 whatever you had, whatever the programs were the trial unit
7 was a necessary adjunct to it because without the trial unit
8 you would not have been able to implement many of the
9 programs.

10 MR. SPORKIN: Ben, I think --

11 MR. GREENSPOON: That's the perspective that I
12 have.

13 MR. SPORKIN: Well, the one part that I would add
14 to that, amend it, is that we were facing when we got -- when
15 we started to bring our programs, and as Wally said and Dave
16 said, hit the big people then they of course brought in the
17 big lawyers. They brought in the Edward Bennett Williams and
18 Milt Goulds. And we were there trying cases with people maybe
19 a year or two out of law school and we were getting our clock
20 cleaned in the courthouse.

21 And so, therefore, Irv and I discussed this and I
22 said we got to have a trial unit. And Irv's going to finish

1 this and he's going to tell you about we almost -- and I said
2 let me try and do it, Irv. And Irv said you're going to have
3 a revolution. And we did have a revolution because he thought
4 that would hurt the people that were there and their spirit.
5 And we did. We had a very tough time. But I think we, we
6 overcame it and it worked out pretty well.

7 Do you remember those days, Irv?

8 MR. TIMMENY: I always thought it was very
9 important to remember that when Edward Bennett Williams came
10 in he owned the Redskins at the time.

11 MR. SPORKIN: Oh, Jesus.

12 MR. TIMMENY: Stanley would often begin the meeting
13 and maybe take up about 98 percent of the meeting by telling
14 him who should play quarterback. I remember Stanley often
15 saying that maybe there should be an improvement on guard. Ed
16 Williams got a lot of advice from Stanley about football.

17 MR. GREENSPOON: Listen. When I had the Gulf and
18 Western case with Ed Williams he by that time owned the
19 Orioles. And I, I gave him a lot of good trades none of which
20 he did because they won the pennant and the World Series
21 without my help. But those were the kind of lawyers we were
22 running up against, guys that owned baseball teams.

1 MR. DOHERTY: I don't think this panel should
2 complete its discussion of trails without talking about Bob
3 Laprade's work.

4 MR. SPORKIN: Oh, Jeez.

5 MR. DOHERTY: He was the --

6 MR. SPORKIN: The trial unit.

7 MR. DOHERTY: -- beginning and end of the trial
8 unit.

9 Stanley may have forgotten this but I started in
10 the Washington Regional Office and then I thought I would
11 transfer to headquarters. So Stanley said that I should come
12 over because he had this concept of creating a trial unit, and
13 Bob Laprade and I could start the trial unit. And it went on
14 from there. Bob was there from the beginning and he tried
15 cases everywhere.

16 MR. TIMMENY: Well, let me go back for a second to
17 the review process in the General Counsel's Office. Again
18 this is a matter of perspective. But my perspective at the
19 time was that I believe Harold Williams was the chairman, and
20 Chairman Williams wanted to hear another voice other than the
21 Enforcement Division voice on all enforcement matters. And it
22 was at his initiative that this review process I think was set

1 up in the General Counsel's Office.

2 And if you take that back even another step I think
3 for a number of years through the '70s whenever a chairman
4 came in the Senator Harrison Williams who was over on the
5 Senate side and as the head of our oversight committee would
6 extract a blood oath.

7 MR. SPORKIN: No, no, it was Proxmire.

8 MR. TIMMENY: No, Proxmire was on the --

9 MR. SPORKIN: Yes, Proxmire used to get the
10 promise.

11 MR. TIMMENY: Well, I thought --

12 MR. SPORKIN: Williams wanted to see me go. No,
13 no, you've got that wrong.

14 MR. TIMMENY: Harrison Williams -- No, I don't have
15 it wrong. Let me finish. Times have not changed, guys.

16 (Laughter.)

17 MR. TIMMENY: What had happened was that Williams
18 would extract a promise from the chairman, from the candidate
19 for chairman --

20 MR. SPORKIN: To fire me.

21 MR. TIMMENY: -- that he would control Stanley.

22 MR. SPORKIN: Oh, I see. That's right. That's

1 right.

2 MR. TIMMENY: Proxmire would extract the promise
3 that Stanley would be given a free hand. So it's back to the
4 process.

5 MR. SPORKIN: I would not be fired.

6 MR. LEVINE: Can I add one element to this?

7 MR. SPORKIN: Let's do. I forgot where you were
8 going.

9 MR. LEVINE: Getting away from Stanley being hired
10 or fired. And that is if you looked at the relationship of
11 enforcement or regulation in the middle '70s up to the point
12 when Harold Williams came in, which will tie into this review
13 process, enforcement played an inordinate role in the
14 formulation of regulations. And I mention four things:
15 beneficial ownership definitions, tender offer regulations,
16 going private and perks, all of which were regulatory
17 initiatives in the '70s I believe, most of which took place in
18 the middle '70s. And I see people in the audience.

19 And the enforcement not only because of the cases
20 it brought but also it had a strong voice in the direction of
21 the regulatory initiatives coming out of that which were
22 negotiated both at the Commission and at the staff level and

1 enforcement played an exceedingly strong role.

2 One of the things that Harold Williams wanted and
3 the Commission wanted was to take enforcement back out of
4 having such a large influence in that scheme. And one of the
5 ways of doing it, particularly when the new general counsel
6 came in after Harvey left in '78, was to have the general
7 counsel play that role rather than enforcement. And I think
8 that impacted not only the review enforcement cases but also a
9 lesser role.

10 And I think today probably the enforcement group
11 plays a lot different role relative to a regulatory scheme
12 than it did when we were there at that time.

13 MR. SPORKIN: Yeah, General Pitt, I mean Chairman
14 Pitt was always supportive. He would bring me in to try some
15 of the cases. So I don't think -- I think it came after,
16 sometime after him which we won't finger where it went.

17 But in any event and it wasn't the general counsel,
18 it was the fact that the Commission was trying to rein us in
19 because they found that, and it wasn't Harold Williams, it
20 actually started before him that they got themselves so
21 involved in these programs and in criticism and they felt that
22 they had no control.

1 Let's take the payments program for example. The
2 payments program we started down in the division finding that
3 after the -- during the Watergate hearings you had companies
4 testifying about making illegal campaign contributions. And
5 as we usually did I would call in, I called in Bob Ryan. And
6 Bob, I said, Bob, go over to Gulf Oil and find out how they
7 made that illegal campaign contribution. And of course he
8 came back and told me that they had the secret slush fund of
9 \$10 million and they were making all kinds of contributions.
10 And of course we started to bring cases.

11 Well, the Commission didn't know where we were
12 going. And so long as they didn't -- and you didn't know
13 where we were going but we were going. And we would --

14 PANELIST: The Commission didn't want to go there.

15 MR. SPORKIN: Yeah, they didn't want us to go
16 there.

17 So we went on and on and on until -- and, you know,
18 you talk about today's atmosphere with corruption, well, we
19 had corruption that was beyond belief. There were 650
20 companies were making these illicit contributions. And they
21 were not only campaign contributions but they were bribes
22 being paid in overseas matters. And then when people would

1 say, well, that's overseas, you know you don't have to worry
2 about it, we found that they were bribing milk producers here
3 in the United States. We found all kinds of perks. You talk
4 about perks now.

5 But we got a little too far when they started, when
6 someone brought a case against Playboy, Hefner because he was
7 expensing the towels of his mansion I thought even we were
8 going a little too far that they had to disclose what he was
9 doing in the confines of his bedroom and why he needed so many
10 towels. But and --

11 MR. SONDE: Who investigated that?

12 MR. SPORKIN: Oh, well, the point was that one day
13 Alan Levenson and I were down in, we were down in Texas and we
14 got a call that we had to come home right away. Ray Garrett
15 was the chairman then. And Ray said, look, Stan and Alan, --
16 I'm glad Alan took some of the blame, why I don't know,
17 because he's just a good guy -- but the chairman said, you two
18 guys, and I guess Irv was involved too, he said you guys go
19 out and fix this problem, I don't want to see, you know, too
20 many more cases.

21 And that showed the creativity and that's how you
22 got the volunteer program which seems to have been dusted off

1 now and is now being used a little bit by -- but not now, it
2 can't be used now because of the atmosphere, there's no
3 volunteers anymore.

4 MR. SONDE: It's called cooperation.

5 MR. SPORKIN: You get shot at now if you volunteer.

6 But that started the volunteer program where Alan
7 had a, you know, Alan and I sat down and to Alan's great
8 credit we came up with this program and it worked. And so we
9 got, what did we bring, we brought, we got about 650
10 volunteers that came in under that program.

11 MR. POLLACK: Well, the importance of all the
12 things you're discussing show how important it was for
13 enforcement to really be the moving force. For despite the
14 Commission's reluctance to go for legislation your intimate
15 relationship with Senator Proxmire resulted in the Foreign
16 Corrupt Practices Act.

17 MR. SPORKIN: That's right.

18 MR. POLLACK: So you see that, and I mentioned in
19 the earlier panel, you see it again today in the Sarbanes
20 legislation. The enforcement or the lack of enforcement is an
21 impetus toward getting policy moving in the proper direction.

22 I'd like to get back to what you mentioned though,

1 Ted, on the pendulum swinging as it did so that the courts did
2 not support the agency, you're absolutely right, in the manner
3 that it had before. What I'm wondering about was it because
4 you think it was punitive actions alone or was it just a
5 change in the composition in the Supreme Court and in the
6 lower courts that caused a more conservative attitude with
7 respect to enforcement and regulation? Because you had, as I
8 look back on it, a movement toward deregulation, the same
9 thing that happened in the late '80s and '90s and then
10 followed up with the scandals and corruption that we've had
11 recently.

12 So it may have been a combination of the both.

13 MR. SPORKIN: Well but, Irv, I think it was more of
14 a very conservative court getting in. Reading --

15 MR. LEVINE: Douglas left and Powell joined in '75.

16 And that, from the Supreme Court level that changed a lot.
17 Timbers left. Timbers was a big supporter of the Commission
18 on the 2nd Circuit. Kaufman, the chief judge, was a big
19 supporter and used to write about the Commission as a special.

20 MR. SPORKIN: Well, we never hurt, we never got
21 hurt too bad in the 2nd Circuit, yeah.

22 MR. SONDE: I don't think you can overlook the fact

1 that when I came to the Commission it was right after Kennedy
2 had been assassinated. A number of us came in the '60s. And
3 we were taught, I was taught that you ought to come and help
4 the government, that you ought to work -- it was a matter of
5 pride to make a contribution to the government.

6 Over the period of time that Ted's talking about
7 the attitude towards the government, it doesn't matter whether
8 you talk about Republicans or Democrats, civil servants were
9 the bashing boys that it was no longer -- they were lazy, they
10 were corrupt, there was fraud, there was this, there was that.

11 There was never anything here like that but in fact that was
12 the tone.

13 And I think part of that started to influence the
14 way in which the Commission was received in the courts and I
15 think also it was the change. But I think that that, that had
16 a real impact on the way in which we were perceived in the
17 government for 20 years whether you go back to Carter, who ran
18 against it, or Nixon. You know, the great thing I think,
19 Stanley, that happened is Hamer Budge was here before Nixon
20 took office so that he could at least in some way protect,
21 frankly, --

22 MR. SPORKIN: Right.

1 MR. SONDE: -- you and Irv and some of us from the
2 political process that I think would have --

3 MR. SPORKIN: Well, you know, one thing that we
4 ought to talk about for a minute is, this was raised by Dave
5 Silver in the last, the one thing that Irv and I insisted upon
6 was that we didn't want this to be an ad hoc, case by case
7 program, and that we did want to see permanent change which
8 was brought about by certain things that were done.

9 And let's look at some of these things that we
10 believe the enforcement program was responsible for. Talk
11 about corporate governance, David. We are now going through a
12 new phase of corporate governance. But don't you think that
13 the Foreign Corrupt Practices Act brought the federal
14 government into corporate governance at an early stage?

15 MR. DOHERTY: I don't think there's any question
16 about it. Certainly in our programmatic approach we always
17 try not only to catch the people that are engaged in the
18 violations but long term we want to try to get the problem
19 fixed. And what we saw in those cases was a lack of integrity
20 in the books and records of the firm and that bore on the
21 integrity of the management of the firm. And sometimes it
22 bore on the quality of the earnings.

1 And so with the background we put together in those
2 cases we were able to get the Foreign Corrupt Practices Act
3 passed and that really did get you right into the corporate
4 governance area. There were mandates to maintain internal
5 procedures and controls and the like.

6 MR. SPORKIN: Irv and Ted, takeover legislation, is
7 my recollection correct that it was we in the division that
8 were instrumental in bringing that about? Because as I recall
9 we had tremendous opposition among the lawyers in the bar. Do
10 you have any recollection on that, Ted?

11 MR. LEVINE: Well, I think you're right but --

12 MR. SPORKIN: The 5 percent rule and if you make an
13 offer you've got to treat everybody fairly?

14 MR. LEVINE: Regulation 14(d) is what you're
15 referring to came out of the --

16 MR. SPORKIN: The Williams Act.

17 MR. LEVINE: Yeah, the Williams Act. But that also
18 and also the SEC v. Beckton Dickinson and the Wellman case in
19 defining tender offer, the defining beneficial owner which was
20 a much more expansive definition than ever before all came out
21 of abuse in the enforcement program by and large. I mean and
22 it was joined with the other divisions and that led to either

1 legislation or regulatory reactions.

2 So I think there was a great role. And enforcement
3 was used as the laboratory to identify problems which the
4 regulatory scheme would then use to fix. That's the way I
5 remember the system. And we used to use that, the approach.

6 Going private is another perfect example. I mean
7 when Al gave that speech, I think it was in '74, nonetheless
8 we had all these problems with going private cases and that
9 led to the growing private regulatory scheme, I think it was
10 13e-3, whatever it is I don't remember now. So I think you
11 had all that.

12 But the interesting thing on governance is that the
13 Commission itself was schizophrenic.

14 MR. SPORKIN: Right.

15 MR. LEVINE: In 1978 the Commission, as I recall,
16 proposed that you had to have internal controls discussed in
17 your annual reports. And there were 900 letters received in
18 opposition and it was dropped, if you recall that.

19 And also there were speeches about what we give
20 today as given, there were speeches by commissioners saying we
21 shouldn't disclose the difference between independent and non-
22 independent directors because it could put a negative

1 connotation on non-independent directors. So I think it
2 wasn't a picture where we had a unanimous support at the
3 Commission for governance change. It was so we used cases and
4 I think the public persuasion to get it done. That's my
5 recollection.

6 MR. SPORKIN: Irv, what is your recollection on
7 that?

8 MR. POLLACK: Well, I think it's right. It
9 reaffirms what the first panel and this panel have been saying
10 that when you go up against the establishment and you try to
11 change basic operations that have been going on purportedly
12 among your reputable industry, as people will assert, it's
13 very difficult to do that.

14 So how to you counteract that? You counteract that
15 by making investigations and showing that the practices are
16 not as honorable as they are described. And I think that you
17 again see that in its most aggressive form in the recent
18 period that we've had.

19 Once the disclosures and the enforcement show
20 tremendous corruption in terms of your so-called reputable
21 industry, even if it is only a small part of it, creates an
22 atmosphere out there that is terribly detrimental to the

1 confidence that people put in the marketplace. Remember, for
2 many years our enforcement, regulatory and disclosure program
3 was considered the best in the world. People all over the
4 world were envying it. Nobody could attack our rules on
5 financial statements because purportedly the rest of the world
6 did not have as good an oversight on accounting things.

7 And just in a few years with a few scandals that
8 were notorious in their extent and in the corruption and in
9 the misconduct by CEOs and in the auditing and the
10 professional areas and by the investment analysts and in the
11 self-regulatory schemes that were there, for example, the
12 NASD's failure to control the over-the-counter market, all of
13 those things resulted in what never would have happened
14 before. And now it's the legislation that has swung the
15 pendulum the other way.

16 Back to something that you said. It was a
17 reluctance to do things because everybody said you're
18 interfering with states' rights, you're interfering with the
19 states' settling of the ethical standards or the regulatory
20 standards for directors. Now you can read the results of the
21 Enron disaster in an article by the Vice Chancellor in
22 Delaware who writes a very comprehensive and excellent

1 analysis saying that the states now have to reexamine the
2 respect that they previously gave to so-called independent
3 directors. Now that's a revolutionary statement. And he goes
4 through and shows in example after example how just saying
5 that you rely on independent directors may have been a
6 misapplication because people are not that independent as
7 events have shown.

8 MR. SPORKIN: Ted, let me, let me, I'm going to
9 give you a question then you can ask it.

10 Let me point out one of the things we did was not
11 only did we assist the Commission but we created certain
12 nomenclature. Greenmail, Ted, I always thought that that came
13 about during a meeting that either Wally and you and I or Ed
14 Hurley had and that we came up with the name greenmail. Is
15 that your recollection?

16 MR. LEVINE: Yes, it is my recollection because how
17 can I disagree with you. But I don't remember who was there.

18 MR. SPORKIN: Yeah, that's in the dictionary now.

19 Wally, do you remember that at all? No?

20 MR. LEVINE: The one thing I wanted to -- because
21 it did happen that way -- but the one thing I want to say
22 about Irv, Irv, in the Foreign Corrupt Practices Act before

1 the Commission drove legislation. Here in the Sarbanes-Oxley
2 I don't think the Commission drove that. I think Congress
3 drove it and forced the Commission now to adopt a lot.

4 And I think that's a big difference where the
5 determination of legislation where we were doing this was
6 really coming from the staff of the Commission actually or the
7 Commission. Now it's being foisted upon the SEC more. And if
8 you see these timetables that in six months they've got to
9 adopt this, four months this, whether they liked it or not I
10 can't tell but I didn't think they controlled the destiny of
11 the agency quite frankly in that regulatory battle.

12 MR. SPORKIN: Ted.

13 PANELIST: They did not.

14 MR. SPORKIN: On the Corrupt Practices Act it was
15 Congress coming to us. The Commission didn't want to do
16 anything on that.

17 MR. LEVINE: Well, no, the staff did.

18 MR. SPORKIN: What? Oh, the staff wanted to do
19 something. Yeah, the staff. Of course we wrote it. It was
20 Sandy Burton that did the controls and the internal controls
21 and I did the --

22 MR. LEVINE: Right.

1 MR. SPORKIN: -- books and records. But the
2 Commission was against that. They said we didn't need it, and
3 we did need it.

4 But let's go on a little bit.

5 MR. TIMMENY: One point before you go on, Stanley.
6 On this corporate governance issue there's no question we
7 were involved in a payments program, we were interested in
8 corporate governance. If you remember the key word we used
9 over and over again was stewardship. We went to the
10 Commission on each and every case and said the issue here is
11 the stewardship of the offices and directors for the use of
12 the assets of the shareholders. And we came at that over and
13 over and over again.

14 And it was our goal to try to do something about
15 corporate governance. Now, we had to use the tools that were
16 available to us which would be the disclosure mechanism
17 because obviously the SEC did not regulate the activities of
18 officers and directors as would the states. So but the
19 direction throughout that program was corporate governance.
20 We were definitely aimed at trying to see to it that the
21 persons who were charged with stewardship for the assets of
22 the company disclosed how they were using those assets. We

1 were more focused on that than we were on the so-called
2 corruption, if you will.

3 The fact that the prince of someplace got a payment
4 or the premier of Japan was involved in something was only
5 part of our focus. Our key focus was how was the money being
6 managed by, you know, on behalf of the shareholders by the
7 officers and directors? So it was definitely a corporate
8 governance direction and it definitely came from the Division
9 of Enforcement.

10 MR. SPORKIN: Let me ask you on insider trading,
11 Ted, and I see Paul Gonson is in the room, inappropriate
12 theory how did that come about? Was that, that was mostly
13 general counsel or was that? How did that come about, Paul,
14 do you remember?

15 MR. GONSON: Well, Ted will remember as well too it
16 was that --

17 MR. SPORKIN: You want to come up and just get on
18 the microphone here. You're going to have trouble.

19 MR. TIMMENY: You're a guest speaker.

20 MR. SPORKIN: Because I think that's one of the
21 most important, that was one of the most important legal
22 accomplishments that we've ever had in the insider trading,

1 wasn't it, Irv, the misappropriation?

2 MR. GONSON: I'm just now paraphrasing Ted Levine
3 who is here of course to speak for himself, but I think it was
4 the combination back in the late '60s and the '70s of the rise
5 in takeovers and also the rise in options. So you were having
6 situations where one company is going to take over another
7 company and by use of options you could leverage enormously.
8 So put down a little bit of money you could really make a huge
9 bundle if you had inside information on a takeover.

10 And the theory that was in existence then which was
11 officers and directors owed a duty to their own shareholders
12 not to disadvantage them didn't apply. You were now talking
13 about securities not of your own company but securities of
14 another company, the company about to be taken over. So there
15 developed another theory which was a theory, first it was
16 called, you may recall some of us used the phrase market
17 access or market information as distinguished from inside
18 information. The Supreme Court rejected that distinction and
19 said no, there's just one theory.

20 But eventually the theory developed that if you
21 were defrauding the source of the information as distinguished
22 from people in the market that also is a violation. That's

1 how this developed.

2 MR. SPORKIN: Well, did that come about was it your
3 creation as General Counsel? Or I guess what you're saying it
4 came out of one of our cases that we developed but you had to
5 go and defend it in the Court of Appeals and we had to come up
6 with -- Does anybody know where the first wording of the
7 misappropriation theory?

8 MR. LEVINE: It came out of Chiarella. It came out
9 of Chiarella. After the Supreme Court decision in Chiarella
10 the program was a great loss. And we did two things, we
11 adopted 14a-3, a rule to deal with tender offers, insider
12 trading tender offers, and we started developing or looking
13 for an alternative theory. The exact case I don't remember
14 but there were a series of cases in that time period where we
15 had to come up with alternative theories.

16 You were gone.

17 MR. SPORKIN: Oh, no, misappropriation was, that
18 was during my time.

19 MR. ROSENBLAT: Well, of course we lost, as most
20 people here know we lost the Chiarella case.

21 MR. LEVINE: Right.

22 MR. ROSENBLAT: Although the Chief Justice pointed

1 out that it was because we had raised it too late. And he
2 said that if we had brought that up earlier then it might
3 succeed.

4 MR. GONSON: I have a little umbrage at the word
5 "we."

6 MR. ROSENBLAT: "We" being the Commission.

7 MR. GONSON: The SEC brought a civil action against
8 Mr. Chierella and he settled that action and he paid over some
9 \$30,000 in trading profits. There was an Assistant U.S.
10 Attorney in the Southern District of New York who read about
11 the settlement in the newspaper and without advising I
12 believe, I don't think Stanley knew about this until it was up
13 in the Court of Appeals, without advising the SEC went ahead
14 and indicted Mr. Chiarella for the action that the SEC had
15 settled. And he was convicted and the 2nd Circuit affirmed
16 the conviction.

17 And then it went up to the Supreme Court. So the
18 theory on which the case had been presented by the Assistant
19 U.S. Attorney to the jury was a theory which wasn't a
20 misappropriation theory it was sort of the classical theory
21 but it didn't fit. And because it didn't fit the Supreme
22 Court said that Mr. Chiarella owed no duty to the people in

1 the market, he was a stranger to them. He wasn't a fiduciary
2 of theirs, he wasn't an officer and director of the companies
3 he was trading in.

4 And then the government said, well, what about this
5 other theory, the misappropriation theory? And the Supreme
6 Court said that in criminal law as distinguished from civil
7 law you can only affirm a criminal conviction based on the
8 theory presented to the jury otherwise it would be sort of
9 like a directed verdict which you can't have in criminal law.

10 If this had been a civil case then the Supreme Court could
11 have considered that alternative theory because the rule on
12 appeals in civil cases is you can affirm on any basis, even
13 the basis not relied on in the district court.

14 So the peculiarity of this is the criminal case
15 meant the court couldn't reach it. But there were in four
16 opinions of the justices some indication that this might be an
17 acceptable theory in the next case. And it was really the
18 Enforcement Division that was starting to twist those things.

19 MR. SPORKIN: Thanks, Paul.

20 MR. ROSENBLAT: Unfortunately even though the
21 Commission was not the moving force behind the case, the
22 Commission ended up - I think Ralph Ferrara argued the case on

1 behalf of the Commission and pressed the misappropriation
2 theory at that point.

3 MR. SPORKIN: Well, let's talk about another rule,
4 Rule 15c2-11. Does anybody have some, any idea what happened
5 there?

6 PANELIST: Who knows what it is basically?

7 MR. SPORKIN: You don't know 15c2-11?

8 MR. POLLACK: Well, I can tell you what it is.

9 MR. SPORKIN: Yeah. Irv, do you remember what
10 happened there?

11 MR. POLLACK: We tried to put the responsibility in
12 the over-the-counter market for market makers to examine the
13 financials of a company before they started trading in its
14 stock so that there would be some control. And that arose
15 again because we had brought enforcement cases.

16 MR. SPORKIN: Right.

17 MR. POLLACK: And the desire was not to have to
18 bring enforcement cases. If they were trading all that stuff
19 that didn't amount to anything and just trading numbers, to
20 put some responsibility on them. So that was the start back
21 then.

22 MR. LEVINE: Well, the problem though, the problem

1 we encountered is that people went into the market and started
2 making markets in these cases and they weren't responsible,
3 there was no way of breaking a cycle.

4 MR. SPORKIN: Right. Right.

5 MR. LEVINE: And I think we used the suspension
6 actually and the 15c2-11 as a device to get at these two
7 problems which put a burden on the market maker and also to
8 break the cycle.

9 MR. SPORKIN: What happened was that the market
10 makers were trading what they call by the numbers. They
11 didn't want to know what the company was about. They had no
12 idea.

13 We found stocks starting at a few pennies a share
14 going up to \$100 a share. And we asked the market maker,
15 didn't know that the place had no business, had nothing they
16 were doing, it was a complete shell. And so we put in the
17 concept of know your security.

18 In other words, one of the great concepts in the
19 securities area is the "know your" rules. You've got to know
20 your customer and you've got to know your security and many,
21 and other things like that. And that was a concept and it's
22 still again one of the really important rules.

1 These all came about as a result of enforcement
2 work. Not only did we bring the case but we worked with the
3 regulatory divisions in developing the remedy.

4 Let's talk about strategies. One of the things
5 that the public doesn't see is they do not see that when the
6 division was taking action that there was some thought that
7 went into those actions that they were taking.

8 PANELIST: For good reasons.

9 MR. SPORKIN: Well, the access theory, it's now got
10 a new name called gatekeeper. David, what do you know about
11 access theory?

12 MR. DOHERTY: Well, the access theory is really one
13 that's designed to give you the most bang for your enforcement
14 buck. The theory is that when people want to get to the
15 market they can't get to the market without going through
16 certain access points or securing the necessary advice of
17 other professionals.

18 So if an issuer who has got an improper agenda
19 wants to get to the public market he needs professionals. He
20 needs financial services or he needs a broker/dealer or an
21 underwriter. He needs a lawyer and he needs an accountant.
22 And so the theory is that since these people are either the

1 gatekeepers or the points of access to the market these are
2 the places that we would look at very carefully and hold this
3 category of professional to a very high level of
4 accountability for their conduct and thereby control the flow
5 into the marketplace.

6 MR. SPORKIN: In other words there was a program
7 designed to go after the entities that were responsible for
8 the people getting access to the marketplace and that they
9 could control their people. And as a result of that, Irv,
10 that's what you developed in connection with the whole
11 compliance system where every broker/dealer has to have a
12 compliance program.

13 MR. POLLACK: That's correct.

14 MR. LEVINE: Stanley, it didn't develop the way you
15 just described it though.

16 MR. SPORKIN: It didn't?

17 MR. LEVINE: No. It developed because you used to
18 ask the question "Why did this happen?" And really the way
19 access theory developed was when you asked the question "Why
20 did it happen?" you looked beyond simply the entity, let's say
21 the corporation, and you started saying, well, how could this
22 possibly happen? I remember the conversation. Where were the

1 accountants?

2 MR. SPORKIN: That came a little later.

3 MR. POLLACK: That was a little later though.

4 Stanley did this on purpose really.

5 MR. LEVINE: Well, I don't know which agency was
6 that? Was this the SEC or some other?

7 MR. SONDE: No, but, Ted, I think it came out in
8 part because Stanley was asking as Irv was how could this
9 happen in a place like Merrill Lynch or First Boston? Where
10 was the compliance program? Where was the supervisors? Where
11 were -- where was the system in place that would have and
12 should have prevented this? And in effect saying, and I think
13 that's where the legislation came out that basically said you
14 have to have, and if you want credit you have to have in
15 effect a compliance program for the brokerage industry at
16 least that said it's in place. And once you had that in place
17 you in effect had a defense to an enforcement action.

18 I don't think it's ever been successfully utilized
19 but it was that that basically put the compliance program in
20 place.

21 MR. SPORKIN: Well, actually, Irv, I think it was.

22 We didn't have the manpower to police everybody in my

1 recollection.

2 MR. POLLACK: Right.

3 MR. SPORKIN: So we had --

4 MR. POLLACK: Just the Commission.

5 MR. SPORKIN: We had to conscript the private
6 sector. And we wanted to in effect transfer the obligation
7 from the Commission to the private sector. We couldn't bring
8 every case. But in the cases we brought we made sure that
9 those firms would take steps to prevent it from happening
10 again. And that's why you had the whole compliance system.
11 Is that right?

12 MR. POLLACK: Right.

13 MR. SPORKIN: Well, you don't want to say anything
14 else?

15 MR. DOHERTY: Stanley, we really used the same
16 concept in a lot of cases, including the foreign payment
17 cases, where we would do enough investigation to have a basic
18 case but know that we had not done the full investigation that
19 was required. So we would then bring a quick enforcement
20 action and as part of the resolution we would require that the
21 defendant issuer, public company, appoint a special counsel
22 who would be required to undertake, in effect continue the

1 investigation internally with a certain degree of independence
2 so that he or she could do their job and then they would
3 prepare a report and submit it to the Commission.

4 So that was another example of putting
5 responsibility off onto the subject of investigation and
6 freeing up our resources to do other things.

7 MR. POLLACK: The basic theory of the securities
8 laws going all the way back was that the Commission was
9 supposed to be in the background with the shotgun, as Justice
10 Douglas said, and that the industry was supposed to through
11 self-regulation and self discipline in the firms or
12 compliance, as we used to call it, make the system work
13 properly.

14 Today the growth in the industry is exponentially
15 greater than it was during our time. This Commission with all
16 the resources it has is not going to be able to go out and put
17 a supervisor or a policeman in every institution or every
18 business out there that contributes to the marketplace or
19 operates in the marketplace. And so the programs have to be
20 designed to impose on the people who are out there having the
21 direct access to the markets or the direct access to investors
22 to have programs in place that protect the investors and

1 society from mispractices. And, therefore, you are now
2 getting an increasing regulatory imposition on what companies
3 have to do.

4 For example, take just the certification process
5 that now is in place under the Sarbanes Act. It's not just
6 the certification of the documents, it's a whole litany of
7 things that have to be done in order to give a basis for the
8 CEO or the chief financial officer to put his name on a
9 certification that the financials are correct, regardless of
10 GAAP, and that they fairly disclose the company's finances and
11 its operations and disclosures.

12 So the whole emphasis is again to get the
13 disclosures out there, as Justice Brandeis said, the greatest
14 thing you can have in any field is sunlight on what's going
15 on. And you see it in some of the disclosures that are coming
16 out in the present context. For example, look at the impact
17 that the disclosure on the pension given to one of the leading
18 members of the management community which showed how bad these
19 things were getting in terms of the greed that was reflected
20 there. The disclosure did more than any enforcement case you
21 could bring.

22 And I think that our background shows that

1 enforcement is important in sort of being the backstop and
2 getting people's attention that they must obey these things
3 and it's in their self interest to do it otherwise there will
4 be serious consequences that will have personal consequences
5 as well as economic impact.

6 MR. SPORKIN: What would you say, Wally, that you
7 would advise a broker/dealer client about knowing -- Well, let
8 me go two steps. If you were now at the Commission how would
9 you take this compliance concept that we started to the next
10 step? How should the current Commission be using that
11 concept? Do you think they've exhausted the use of it by now?

12 MR. TIMMENY: No, not at all.

13 But let me go back to my understanding of what
14 we're talking about in terms of access theory and so forth. I
15 saw the access theory as a tactic that was employed within a
16 strategy. The strategy, for example, we had an interest in
17 municipal bond cases. Dave and I had, you remember at one
18 time I had come to Irv and Stanley and I said, you know, I
19 read something in the "Wall Street Journal" about these
20 municipal securities dealers in the south who are all called
21 "bond daddies" and they're selling these defunct or these
22 bankrupt issues, bond issues and charging whopping mark-ups.

1 I said, you know, this would be something interesting to look
2 at.

3 So they said, yeah, go look at it. So I went down
4 and I visited a couple of these places and I came back and I
5 said, you know, these shops are really boiler rooms. I'm sure
6 you guys had seen them but I had never seen it. I had ready
7 about what boiler rooms are like but I had never seen them.
8 These shops are boiler rooms, we should do something about it.

9 So they said go to it. So Dave and I went to work
10 on that and we, eventually we brought I would say maybe ten
11 cases against companies and we enjoined 50 individuals and
12 whatnot. And our strategy was to bring enough cases to
13 demonstrate that there was a need for regulation in the
14 municipal securities area.

15 Now, as part of that strategy we brought the cases
16 and then brought that to the attention of the Hill and market
17 reg. and worked out this legislative program. But within the
18 strategy there was a tactic, we also wanted to stamp out the
19 problem as we were going along, and the tactic was to use the
20 access theory. We first went after the dealers who were
21 charging the excessive mark-ups because they provided access.

22 Then we moved over to the underwriters. And then

1 finally we moved over to the lawyers. And that's where their
2 screaming really started because we were trying to bring the
3 lawyers in and have them responsible for the disclosure in the
4 offering statements and for the opinions that they were
5 rendering that these bond deals were real deals as opposed to
6 shams.

7 So I saw, I saw the access theory if you will where
8 you put pressure on professionals as a tactic. The overall
9 strategy was to get legislation to regulate the area. But
10 within that strategy we had the access theory and we went, you
11 know, we put the pressure on the various access points.

12 MR. DOHERTY: To give you just a little color and
13 background on that, when we went down to actually litigate
14 some of these cases and we went down to file our action, in
15 federal court in Memphis against some of these bond daddies
16 and as is customary I stopped into the U.S. Attorney's Office
17 as a courtesy to let him read the complaint before I filed it.

18 And the complaint really was a classic boiler room,
19 outrageous, just classic, with mark-ups over contemporaneous
20 costs in these bonds in the vicinity of 25, 50 and 100
21 percent.

22 And he read the complaint and he said to me, "Well,

1 I don't think you've got much of a case. You know I don't see
2 that this is much different than a used car salesman. You
3 sell your product for what you can get, so I don't think
4 you're going to have much luck in there."

5 Fortunately the judge saw it differently. We tried
6 the case and won. We did end up going to Congress because at
7 that point dealers who dealt exclusively in municipal bonds
8 were exempt from registration as broker/dealers with the SEC.

9 And we'd never dealt with municipal bond dealers before. And
10 so we ended up getting legislation. The exemption was removed
11 and the problem went away.

12 MR. SPORKIN: Now, one thing, Irv, that we, that
13 our problem was that we didn't have all the nice toys that the
14 current enforcement group has. We couldn't go and get bans on
15 officers, directors. We had trouble, you know, getting fines
16 or getting money back. Ted, did that stop us? What did we do
17 about it? Did we just say, ah, we can't do it so we'll go
18 home?

19 MR. DOHERTY: I have a case right here where we did
20 it in 1975.

21 MR. SPORKIN: Tell me about the case, David.

22 MR. DOHERTY: It was SEC v. Techniculture, Inc.

1 MR. SPORKIN: And what happened.

2 MR. DOHERTY: This was a shell promoter who
3 violated over and over --

4 MR. SPORKIN: Right.

5 MR. DOHERTY: -- again and we went out and we got
6 an injunction against him. And the judge also enjoined him
7 from assuming a position as or continuing as an officer or
8 director of any public company unless he said so.

9 MR. SPORKIN: What do you think of that? Did you
10 know about that?

11 MR. LEVINE: In the interest of full disclosure --
12 Stanley, the use of, to me the greatest tool in the modern
13 enforcement arsenal was the consent without which the program
14 would either back when we were there or today could not
15 function as a practical matter. And the consent gave you the
16 ability and actually as part of that or to develop different
17 ways of getting remedies that you could not specifically look
18 to the statute to get.

19 And if you settled 80 percent of your cases at all
20 times or 90 percent, which we did, you were able to meld the
21 theories of what we wanted to do and put it into practice in
22 the consent because once you had the violation and you were

1 trying to be remedial the consent gave you that, whether it's
2 back in Vesco or Parvin Dorman or Westgate it just gave you
3 the -- it was only the creative mind that could come up with
4 the relief, whether it was disgorgement or things like that.

5 So I, to me the greatest thing we had was the
6 consent and still is today.

7 MR. GREENSPOON: Well, that's of course what made
8 the remaining 10 percent of the cases that we had to try so
9 awful.

10 (Laughter)

11 MR. LEVINE: Well, you only tried the bad cases.

12 MR. GREENSPOON: Well, of course we had to try the
13 bad cases.

14 I think what we did our won/lost record was sort of
15 like the Orioles today.

16 MR. POLLACK: What we did was we used the power of
17 the courts to extend the statutory grants of power. First
18 cases we did we said the court can appoint a receiver. SEC
19 may not have that authority but the court could do it.

20 The next step was once you had a good case the
21 court could order restitution. And we emphasized that once
22 the SEC was in there and got a decree it wasn't the SEC's

1 decree anymore it was the court's decree. And so you, Your
2 Honor, can use the decree not only to stop these scoundrels
3 but to give the money back.

4 MR. SPORKIN: And disgorgement the same way.

5 MR. POLLACK: Disgorgement the same way. And so
6 that approach was used. It gets back to what you said much
7 earlier in this program though, we had a reception in the
8 courts that I think in the late '80s and certainly in the '90s
9 reversed itself and the courts did not understand or at least
10 appreciate the program's policy and the policy of the statute
11 to protect the public. And so they looked at this more like
12 it was some negligence case out there where two private
13 parties were performing.

14 I think you've got to improve the culture out there
15 so that the people who really control the industry, the
16 leaders of the industry create that culture for the people
17 below them.

18 MR. SPORKIN: So we were able to accomplish many of
19 the things that the Commission today is able to accomplish
20 although they are doing it with specific authority. We did it
21 through the consent decree. Is that your point, Ted?

22 MR. LEVINE: Yeah. Yes, except for two things

1 which I actually think hurt the program.

2 MR. SPORKIN: What's that?

3 MR. LEVINE: One is civil penalty.

4 MR. SPORKIN: Yeah.

5 MR. LEVINE: Because you get disclosure but we
6 didn't have the civil penalty.

7 MR. SPORKIN: Right. Right.

8 MR. LEVINE: And two, I think the C and D can be
9 used, can be helpful but cannot be. In other words, I think
10 it goes both ways.

11 MR. SPORKIN: We used that do, didn't we? Weren't
12 there C and D's?

13 MR. LEVINE: No.

14 MR. SPORKIN: Oh, sure we did.

15 PANELIST: The 21a report.

16 MR. LEVINE: Used 15c-4.

17 MR. SPORKIN: No, we brought out C and D's, I'm
18 telling you. We had by consent. By consent.

19 MR. LEVINE: No, no, even with the consent we
20 didn't.

21 MR. SPORKIN: Yes, we did. We did it with consent.

22 MR. LEVINE: I learned never to disagree with the

1 boss.

2 MR. SPORKIN: I'm telling you.

3 MR. LEVINE: That's one thing we never did. Art
4 Matthews recommended it.

5 MR. SPORKIN: Dan, did we do it?

6 MR. HAWKE: What you would say is you would say
7 that the firm had to agree not to violate the securities laws
8 again. But it didn't say cease and desist.

9 MR. SPORKIN: Well, I'll have to --

10 MR. POLLACK: What the person in the audience Dan
11 Hawke said was that they would include something like that in
12 the decree but didn't say cease and desist.

13 MR. SPORKIN: I remember, I remember we used the
14 words if they would cease and desist. But I'll have to go and
15 look at it.

16 MR. TIMMENY: But you know not all of the progress
17 that we made in terms of ancillary relief was through consent.
18 For example, there was a case that we brought years ago where
19 we litigated a very important corporate governance issue.
20 That was Canadian Javelin.

21 If you remember Canadian Javelin was a Canadian
22 company and we said that their filings with the SEC were

1 improper, inadequate and so forth. And we actually litigated
2 it in the Southern District of New York a provision where we
3 requested the court to appoint a special review person and a
4 person who would specially prepare the filings of the company,
5 require the board of Canadian Javelin to instruct this special
6 review person to do this work and to have this power.

7 And that was actually litigated and opposed. And I
8 argued the motion in front of Judge McMahon. Mike Eisenberg
9 if you recall was the person that we had appointed for that
10 work. And the other side opposed it vigorously and the judge
11 ordered it. And there was an example of corporate governance
12 in the very early stages in the litigated context not in the
13 consent context where we imposed something that was very
14 important in terms of the filing process and it stood.

15 MR. DOHERTY: Actually the Techniculture case was
16 litigated as well and that guy ended up in jail for contempt.

17 MR. LEVINE: There's a quote from Management
18 Dynamics which was a 2nd Circuit case litigated, which I think
19 makes Irv's point, if I could read it where Judge Kaufman I
20 believe said, "The SEC appears not as an ordinary litigant but
21 as a statutory guardian charged with safeguarding the public
22 interest enforcing the security laws and, therefore, we would

1 treat their request for ancillary relief differently than the
2 private litigant."

3 And I think that sums up really the attitude, and
4 this is 1975, of the 2nd Circuit and makes the point as to how
5 we were able to get the relief that someone else might not
6 get.

7 MR. SPORKIN: Yeah. One of the things that the
8 Commission has recently done which I think it's one of the
9 greatest acts of enforcement that I can recall was the
10 recertification. I mean that was brilliant. It defused this
11 whole situation. It made current, it brought everything
12 current. And it was done through use of the provision 21a.

13 Now, to go back to the old days we used to use that
14 21a provision in many different ways. Ted, do you want to
15 start out with it?

16 MR. LEVINE: Yeah. Well, 21a was used actually on
17 the governance side as a way of identifying conduct that we
18 found in cases where the Commission wanted to speak to a
19 general practice but not bring an enforcement matter.

20 Sterling Homex I believe was the first case which
21 was a case that we brought which we sued the company, we sued
22 the underwriters, we sued the accountants. And we used 21a to

1 address the conduct of the directors, they should have known
2 about the fraudulent financials in connection with the
3 offering.

4 But it then went on in a number of cases, Gould,
5 National Student Marketing, there were a whole series of 21a
6 reports culminating I believe with a 21a report written by
7 then Commissioner Loomis, if I'm not mistaken, where there was
8 actually some discussion, and someone can correct me, where
9 Phil Loomis as Commissioner discussed the use of 21a because
10 there was some opposition at the Commission and he actually
11 wrote as part of it. And maybe -- everyone is looking, maybe
12 I dreamt this, but I think there was some contention maybe
13 around Roberta Karmel, it may have been around the time period
14 where there was some question about it.

15 But the Commission used it to develop, to go to
16 Irv's point essentially: here's practices we found which are
17 not appropriate and this is a way of improving conduct. And
18 the Commission used it. And I guess more recently in the
19 Salomon Brothers scandal it was used once again in terms of
20 discussing the responsibilities of supervisors.

21 MR. SPORKIN: The legal issue was that Commissioner
22 Karmel raised was can you -- is it fair to have a 21a report

1 that's non-consensual. And the point there was she thought
2 that the party who was going to get a blast of bad publicity
3 ought to have the right to make a response. Now -- or have a
4 right to say why it should be issued.

5 But we used, as I recall we were pretty creative,
6 we used 21a quite a bit, did we not?

7 MR. LEVINE: Yes.

8 MR. SPORKIN: And, Irv, you used it in the market
9 structure, did you not in hearings?

10 MR. POLLACK: Yep.

11 MR. TIMMENY: 21a was an outlet that was very
12 important for the program. If you remember the New York City
13 report was a 21a report.

14 MR. SPORKIN: Right.

15 MR. TIMMENY: And we brought that because there
16 was, because as you recall there were serious political
17 overtones at the time that affected the investigation. We
18 were conducting an investigation into the sale of municipal
19 securities by New York City. And there were a lot of
20 practices that had gone on that we came up with during the
21 investigation that were serious and had to be treated.

22 But there was also a concern that if we brought an

1 enforcement action it would appear to be directed at the
2 Democratic administration of the City of New York which was
3 then in power. So a 21a report was utilized at that point
4 just to put out a report without any, without a lot of
5 editorial comment about who did right and who did wrong and
6 just lay it out there with all the problems as a mechanism,
7 again, to try to advance reform through legislation. It was
8 all part of this whole municipal bond effort that we had
9 taken.

10 And I thought it was important because I don't know
11 that we would ever have gotten an enforcement case through
12 with respect to the actions of the various politicians and so
13 forth at the time, whereas the 21a report gave us a vehicle to
14 get out there and discuss these issues in great detail and to
15 alert the public to the issues and bring about a cure.

16 MR. SONDE: I think, Stan, what Wally is talking
17 about, and I don't remember a National Student Marketing
18 report headed as such. But I remember with Peat Marwick we
19 did a report which was essentially a 2e proceeding where we
20 got out the practices and tried to reform things by using the
21 speaking vehicle. And 21a was used for that.

22 I don't remember though, Stanley, I mean I think we

1 have to give the current Commission credit for using 21a in
2 which they did in a way which frankly, at least to my memory,
3 I don't think has ever been done before.

4 MR. SPORKIN: Oh, I think it's terrific.

5 MR. SONDE: And that is to require affirmatively
6 the CEOs and the CFOs to certify, something that I don't think
7 had ever been done before.

8 MR. SPORKIN: No, but I think that 21a is one of
9 the most incredible provisions that any agency can have. I
10 think there are still other avenues that you can use 21a.

11 MR. SONDE: Oh, absolutely. But I don't think it
12 had been used --

13 MR. SPORKIN: And I'm not going to tell it now
14 because I want to use it for some of my clients. But that's
15 all right. I will surprise them.

16 But the point was that 21a has so many
17 ramifications, and again to the great credit of the -- sure
18 they can compel someone to make a statement. And before the
19 certificate concept if you recall the Commission went to
20 WorldCom and said we want a report in 24 hours. And what
21 happened? The 21a says you can do it. It give the Commission
22 powers to investigate. It gives the Commission powers to

1 require statements. It gives the Commission powers to publish
2 information. Terrific.

3 But one of the things what I think that reflects
4 back to our time and to the present Commission is the fact of
5 scrubbing through those provisions to utilize every crumb that
6 you can utilize. And we had to use them because we didn't
7 have all the nice toys.

8 But let me give you another area. And, Irv, you
9 probably remember this as well as anybody, the concept of
10 public versus private proceedings. Now, no enforcer in his or
11 her right mind would recommend a private proceeding. But we
12 did and we did it in a way that advanced the program. Do you
13 remember that in the back office cases?

14 MR. POLLACK: Yes. What happened there was
15 industry lost control of its records. And it was a national
16 disaster. And the remedy that we wanted was to get them back
17 in control of their records. So, for example, in the one
18 case, the Lehman case that I recall, Stanley called them in
19 and said you better go out there and hire 50 accountants and
20 get your books and records in shape otherwise we're going to
21 suspend you.

22 MR. LEVINE: They failed, they couldn't reconcile

1 so they failed to deliver because of the volume. And a number
2 of firms got out of sync.

3 MR. POLLACK: It was a circular thing because it
4 affected every firm in the industry.

5 MR. DOHERTY: Everyone was running around the
6 street at the end of the day delivering stock certificates.

7 MR. POLLACK: Yeah.

8 MR. DOHERTY: But the average daily volume on the
9 New York Stock Exchange in 1970 was about 10 or 11 million
10 shares a day.

11 MR. POLLACK: Well, the reason they lost control in
12 those days they didn't have a centralized clearing settling
13 system. Everybody settled with every other broker/dealer he
14 dealt with on the street. The only one that had a program, a
15 centralized one, was the Pacific Coast Stock Exchange. We
16 induced the other exchanges to adopt the Pacific Coast Stock
17 Exchange system to get control over their own settlements.
18 And that was the ultimate solution.

19 But we had to solve the problem in the interim.
20 And in the interim we used the process that I just described.

21 You know, if you look back to the history of the
22 Commission from its start the statute only provided for a stop

1 order proceeding in the registration process. But the staff
2 back then were ingenious and they instituted what was called
3 the letter of comment that exists today, in which the staff
4 would send a comment to the filer and say here's what we think
5 is wrong in your filing and we will give you an opportunity to
6 correct it.

7 And I think using that kind of approach and
8 imagination whether it's 21(a) or it's 15c2-11 or 10b-5 or
9 some other provision was what made the Commission's programs
10 so effective over the years.

11 MR. SPORKIN: On that public versus private, Irv,
12 what happened was when we brought -- we had to actually rack
13 our brains. I recall this. And because we had to do
14 something to the firm but we couldn't disturb the whole
15 industry. I mean we were afraid of the public, there'd be a
16 run on the bank and that would have been catastrophic.

17 And so in those days very few cases were brought
18 against New York Stock Exchange member firms. And so what we
19 did we used to literally look at the law. And it occurred to
20 me it says that the proceedings I think it says may be public,
21 which indicates it may be private. And the theory was, Irv
22 and I, or the strategy was that we said what we'll do is we

1 need something to shake Lehman Brothers up and so we'll
2 institute a proceeding. But what we will do is we will make
3 it a private proceeding so the public won't know right away
4 what's going on.

5 Hopefully we can force them by use of the
6 proceeding to come in and settle it. And that way they would
7 go out and hire 150 accountants, I think it was, Irv, because
8 they didn't have people, bring it into compliance. And then
9 what we would do is then we would announce the proceeding and
10 announce the sanction which was a nothing sanction because
11 they had done everything.

12 And so we used that, we must have used that in at
13 least 10 to 15 cases against major brokerage firms. But
14 that's what you have to do with these statutes. The statutes,
15 that was one of the reasons in the Sarbanes-Oxley bill there
16 are so many provisions in that law that can be used. Now,
17 yeah, it's good to have, obviously it's important that the
18 Congress, you know, gave a message. But you look at 12a under
19 the '34 Act and the Commission has full authority over
20 accountants, over what statement, what the financial
21 statements should contain. Forget about GAAP, they don't have
22 to rely on GAAP, they can set up their own system. It's there

1 in the law. It's never been used.

2 Now, I'm not being critical that the Commission
3 hasn't used it but what I'm saying is it's never been used to
4 deal with this. There are a lot of other provisions in the
5 law.

6 For example, we used to use, and you fellows can
7 join in on this, but suspensions of trading as an effective
8 tool until we got hit a little bit on that one. But --

9 (Laughter.)

10 MR. SONDE: Stanley, I read you were going to
11 private proceedings in Sarbanes-Oxley because all the
12 proceedings that this new accounting board has been after.

13 MR. SPORKIN: Yeah, but that was not, that was not
14 ours.

15 MR. LEVINE: Stanley, we used to bring successive
16 suspensions for maybe a year or two.

17 MR. SPORKIN: Call them rollovers, yeah.

18 MR. DOHERTY: But, Stanley, I think there is a
19 really important point in what you and Irv were just saying
20 about the paperwork crisis papers and that is that we tried to
21 fix the problem.

22 MR. SPORKIN: Right.

1 MR. DOHERTY: There was a large group of firms on
2 the street that were just flat out out of compliance. Their
3 books and records were out of whack, their net capital was out
4 of ratio and a lot of other things were wrong. They had lost
5 control.

6 The easiest thing would have been for us to rush in
7 and enjoin or sue half a dozen New York Stock Exchange member
8 firms. But that wouldn't have fixed the problem. The
9 overriding objective of virtually all the enforcement actions
10 that were brought was not just to sue the person but to fix
11 the problem. And that's what was done there.

12 MR. SPORKIN: And David now runs the program for
13 the New York Stock Exchange so I'm sure he's using many of
14 these strategies.

15 But go back to suspension of trading. I don't --
16 And stop order proceedings. I noticed that the Commission now
17 is using stop order proceedings which they hadn't used before.

18 Now, why would you use a stop order proceeding when
19 you can go get an injunction? It depends upon the facts and
20 circumstances. It may well be that a stop order might be more
21 appropriate than going into a court.

22 Suspension of trading, up until recently the

1 Commission hadn't use that too much. You think it's too
2 little used or you think it's used just right? Ted, what do
3 you think on suspensions?

4 MR. LEVINE: I think the Commission's using it now
5 --

6 MR. SPORKIN: More than they did before.

7 MR. LEVINE: -- more than they did. And they're
8 using it as an appropriate way of stopping. The internet and
9 some of these other scams has created a lot of securities that
10 are floating out there that are worthless. And I think the
11 10-day suspension is a good way of quickly protecting the
12 public where you have that going on. And I think it can be
13 used that way.

14 And also the notice provisions.

15 MR. SPORKIN: Yeah. And I think that's the way we
16 ended up using it.

17 Let me, all right we've got a few minutes left, let
18 us go and ask these questions and everybody just join in.
19 What can the Commission get today from the way enforcement was
20 carried on in your day? Is there anything --

21 MR. SONDE: Stanley, you skip the most important
22 part which is really a dedication to Irv.

1 MR. SPORKIN: What's that?

2 MR. SONDE: Which is the ethical -- and you,
3 frankly -- the ethical lessons that come out of the
4 enforcement program. And you can't do that with this fellow
5 sitting next you.

6 MR. SPORKIN: No. The only reason, the only reason
7 I skipped that was because we discussed it in the last hour
8 about the ethical, you know, the problems we had. I think Irv
9 gave a speech to that. Yeah.

10 Want to give another one on ethical problems?

11 MR. POLLACK: Well, I think it's important not only
12 for the Commission, it's important, it's more important for
13 the Commission --

14 MR. SONDE: But the point, the point is that the
15 two of you were --

16 MR. POLLACK: -- when it is attempting to impose on
17 its regulatory people a high standard of conduct it has to be
18 above that in its own performance.

19 MR. SONDE: Yeah, but I think you're overlooking
20 the contribution, Irv, that you made when you were appointed
21 to the Commission in the face of a scandal in order to restore
22 the integrity of the Commission to the staff so that the staff

1 would believe in the integrity of the process after Brad Cook
2 had to resign as chairman. And, you know, I just say that not
3 as something -- I think it's important to understand the
4 process because we've been through those periods.

5 Stanley himself was involved in a situation where
6 he was basically told by the White House to kill a case and,
7 you know, act appropriately.

8 MR. SPORKIN: I wasn't told but they told us
9 through an intermediary. Is that Vesco?

10 MR. SONDE: Yeah.

11 MR. SPORKIN: Yeah. But go ahead, Irv. I mean we
12 lived through these, we all lived through it.

13 MR. SONDE: But isn't that part of the history
14 then?

15 MR. SPORKIN: Well, Irv, I mean, Wally, you lived
16 through one. What was this, what was your scandal? What was
17 that that you lived through?

18 PANELIST: He hung out on the speakerphone.

19 MR. SPORKIN: Was that your case?

20 MR. LEVINE: Stanley, could I come back to one of
21 the things that you identified early which I think is relevant
22 both today and was relevant when we did it is the fairness of

1 an enforcement program.

2 MR. SPORKIN: You think that that's what the staff
3 can learn today? I think that's a good point you're making.

4 MR. LEVINE: Yes, I think it is.

5 MR. SPORKIN: That's Irv's hallmark.

6 MR. LEVINE: And it is, actually one of the things
7 in preparing for this, looking back one of the things that I
8 undertook in my efforts I found was the redbook, the Guide to
9 Taking Testimony.

10 As you recall, in the late '60s there was no
11 structure within the division of what the rights are. And we
12 created in fairness to the respondents a whole what was called
13 the redbook, I think it may still be the redbook, I don't know
14 today, where we put out a whole guide to our staff on how to
15 comport itself relative to conducting investigations. And I
16 think this notion of being fair given the power we had was one
17 of the hallmarks of what I think Irv and Stanley promoted.

18 And I think a lesson could be learned today or it
19 should continue.

20 MR. SPORKIN: In other words, here, this is the
21 time that really the staff and the Commission has to use
22 restraint more than ever before because they've been given all

1 this new power and there's nothing that's going to stop them.

2 They've got powers now that in this culture it's going to go
3 through and the staff does have to and the Commission does
4 have to use restraint.

5 MR. GREENSPOON: I'd like to add one thing to that.

6 And I think it's something that permeated the years that I
7 was in enforcement and that is the use of a very uncommon
8 attribute called common sense. And I have found that many,
9 many times a zealous attitude overwhelms common sense.

10 And I think that one of the greatest things that
11 the Enforcement Division at least demonstrated to me was the
12 use of common sense. I had been in the private practice of
13 law for 20 years before I came here, as you may recall. And I
14 found that by and large for the most part common sense was
15 exercised in great abundance. And I think that one of the
16 greatest legacies that any of us who were there have passed on
17 is the use of common sense in investigations and in treatment
18 of people, conducting the investigation, fitting right in with
19 Ted's views on the so-called redbook.

20 MR. TIMMENY: We do distinctions in the Enforcement
21 Division. When we were recommending a case to the Commission,
22 cases to the Commission we were not on autopilot. In other

1 words we did not say that every person who had a brush with
2 the problem had to be dumped into a case. We tried to bring
3 cases that made a lot of sense because the people who were
4 truly involved were included in the cases.

5 And we tried to bring common sense, as Ben said, to
6 the range of charges that we brought. That was important
7 because we had to have credibility. We had to have
8 credibility with the Commission, we had to have credibility
9 with the bar when we brought these cases. So there was
10 definitely an effort to approach a case in a way something
11 other than automatically trying to bring every single charge
12 that you could bring or every single person that you could
13 bring. And that was highlighted especially in the foreign
14 payments.

15 MR. DOHERTY: I would just extend that a little
16 bit. I think that the staff has to feel that they can be
17 aggressive. There's a lot of work to do and they must feel
18 that they will be supported if they are aggressive. There
19 must be balance with fairness. And it's much easier, frankly,
20 to be aggressive than it is to be fair. It takes a certain
21 amount of experience and security in yourself or your managers
22 to make a decision not to sue someone just because it doesn't

1 need to be done. It's easier and safer to be aggressive.

2 MR. SONDE: I remember, Stanley, exactly what

3 Dave's talking about. I remember a case that was not a case.

4 You had brought a case against a number of the institutions

5 and senior people and then there was a young kid who had gone

6 to the finest schools who had basically learned to launder

7 money. And instead of suing this kid you brought him into

8 your office and you had a face to face conversation with him

9 but basically you told him we were going to give a pass. And

10 you told him all of the blessings he had gotten and brought a

11 non-case.

12 And to me that was one of the finest things.

13 MR. SPORKIN: The day I arrived as a lawyer I felt

14 good about it, Irv, at the time that I had recommended the

15 suit of a lawyer who was a compliance director in a firm and

16 that when I looked at the facts I learned that he had told his

17 boss not to do something. And we had an aggressive staff that

18 insisted that we name him because he didn't do enough, he had

19 to quit. And I thought that was asking too much to require

20 him to quite a job.

21 So after the Commission had authorized the action

22 and we were about to bring it I told Irv I was going to go

1 back to the Commission and say that my conscience would not
2 permit me to sue this person. Irv said go ahead. And we
3 dropped that person from the lawsuit.

4 That's when you know that you've arrived when you
5 can do something in that vein.

6 But let me say this, and I guess we've got about a
7 second left, what I am so ecstatic about in this day and age
8 is that first of all there is tremendous support out there for
9 the Commission and the enforcement program. The Enforcement
10 Division has good people -- and I'm being self-serving because
11 my son's there -- but I'm talking about right up to the top
12 and the Cutlers and the Thompsons and all the rest of the
13 people all the way down.

14 Now, but even more important, not more important
15 but as important is you've got a fantastic Commission now.
16 And I am so proud to see this Commission with the intellect
17 that's there now, it is absolutely incredible. And there
18 ought to be some really great things happening.

19 I think you saw what happened with the
20 certification how, you know, nobody gives the Chairman of the
21 Commission any credit for what they do but look how that
22 defused this terrible situation out there. You don't hear

1 people talking anymore about, you know, companies folding or
2 whatnot. I mean before that day in August everybody thought
3 the whole, the whole community was going to -- the whole
4 financial community was collapsing. And that thing really
5 calmed things. It was a brilliant act. And you're going to
6 see a lot more brilliant from this Commission. But I do think
7 what our panel said, Irv, that fairness is still a very
8 important thing.

9 What do you think to conclude?

10 MR. POLLACK: Well, when somebody used to come and
11 ask whether something is legal to do we used to say that's not
12 the question you ask. The question isn't is it legal to do
13 it, but is it fair to do it? That's the standard that you
14 want to apply. And I think that is why the Enforcement
15 Division can be aggressive in its programs and yet accomplish
16 respect from the people it sues. By attempting to get them to
17 improve their operations it can make it easier for them to
18 make a good profit in their business and at the same time
19 serve their customers and society well.

20 MR. SPORKIN: Well listen, I thank you people that
21 have stayed with us, you're terrific that have been here. And
22 we hope you've enjoyed it. I hope enjoyed it as much as I've

1 enjoyed it.

2 MR. POLLACK: And the panelists.

3 MR. SPORKIN: All the panelists, I told them
4 they're going to see the A material here.

5 MR. POLLACK: Thank you very much.

6 MR. SPORKIN: Thank you.

7 (Whereupon, at 5:00 p.m., the Roundtable was
8 concluded.)