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CRISIS AND THE CORPORATE COMMUNITY

ADDRESS BY

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COMMISSIONER

SECURITIES AND EXCHANGE COMMISSION

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## CRISIS AND THE CORPORATE COMMUNITY

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We are in the midst of another chapter of what has been a sordid time in the lives of all of us. This time has been trying because it has been a time when beliefs that we had entertained concerning ourselves, our nation, our government and our economy have been dented, undermined and in part, destroyed. It is always a painful experience to have our illusions shattered, to have placed alongside them what is really real and find that the “reality” we had cherished was in large measure illusion.

Until very recently most of us took deep pride in the belief that in this nation we had erected a governmental structure that was free of the gravest defects of governments through history. We had a government in which the exercise of power was closely reined and subject to considerable constraint. We thought we had bred a new kind of statesman, a new kind of leader, the kind of leader who would have ingrained in the deepest fibers of his being respect for these restraints and for this tradition that had been so arduously carved out of history and out of the raw land of this country. We believed that while money still played a larger than desirable part in our political processes, it had been tamed and its influence reduced so that the affairs of the nation were not significantly subject to the whims of those with the biggest bank accounts.

Similarly, we believed in the integrity of our business leadership and the efficacy of the disclosure and financial accountability processes that we had so carefully

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nourished and brought to nearly full bloom under the watchful eye of the Securities and Exchange Commission. We were confident that the resources of American corporations were being administered by managements acting as stewards for the shareholders, and that these stewards were “playing by the rules” and making sure that the books of the corporation were not “cooked” or jockeyed about like those of a tax-dodging corner merchant. Notwithstanding misgivings increasingly expressed about the manner in which multinational companies, most of them based in this country, were conducting themselves, we nonetheless felt confident that our business leaders, among the prime beneficiaries of our freedoms and brought up amid the traditions of this country, were above venality, deceit, concealment, subterfuge and just plain bribery no matter where they conducted their affairs.

In the last two or three years, we have indeed lost our innocence; we have in a sense known sin and been repelled by its face. We have learned through harsh experience that an unworthy man could reach the lofty position of Vice President of the United States, climaxing a political career known now to have been characterized chiefly by payoffs, bribery, income tax evasion and betrayal of public trust. We have witnessed in horror the misuse of power and the turning of it with vengeance and with venom against hapless citizens who dared to cross the wishes of those who had the power, a power it should be noted bestowed by the people. We have been shocked at stories of alleged involvement by governmental agencies in all sorts of questionable activities: political assassinations, break-ins, wiretappings, imposition of LSD upon unsuspecting victims and a dozen other abuses of power.

Among the most distressing of disclosures has been the revelation that many large corporations have engaged in a variety of misdeeds and questionable deeds to an extent never imagined. Our first introduction to this phenomenon occurred when the Special Prosecutor discovered in the course of his investigation that a number of American corporations had contributed substantial amounts of money to the Committee to Re-elect

the President in 1972. I think that when these charges first surfaced, most of us believed that indeed the corporate officials were more to be pitied than censured. It was thought that they had been the reluctant victims of arm-twisting by over-zealous fund-raisers of a, by the time of disclosure, largely repudiated President. We heard stories of executives to whom it was strongly intimated that unless substantial contributions were forthcoming, various governmental favors would be withheld or governmental retributions inflicted. However, as the stories unfolded, it became apparent that this notion was perhaps our last effort to hold fast to our illusions. We learned that in some instances the pattern of illegal political contributions extended back many years and involved far more than the amounts contributed in 1972. In many instances these contributions were carefully planned, artfully concealed and in no sense the fruit of illicit pressures. The means of tucking the money away for future distribution were often carefully developed, with clear assignments of responsibilities and well-developed techniques for the bestowal of the favors.

The most distressing aspect of all this -- more distressing, if possible, than the realization that many corporations had deliberately, knowingly, wittingly, and as the result of command from the highest levels, flaunted the American election laws -- was the discovery that frequently these payments were made out of substantial pools of money that had been sucked out of the corporate accountability process and squirreled away in the accounts of overseas agents, Swiss bank accounts, Bahamian subsidiaries, and in various other places where the use of the money would be free of the questions of nosy auditors, responsible directors, and scrupulous underlings. These systems were characterized by such interesting phenomena as the transportation in suitcases of vast sums of money in one hundred dollar bills by top executives. False or misleading entries were made in the books of corporations to conceal the true purposes for which the money was used. In virtually all of these cases, it was impossible for top management to shield themselves from full responsibility. These were not cases of fawning subordinates trying

to win executive suite favor. Rather it was the executive suite itself which was engaged in deceit, cunning and deviousness worthy of the most fabled political boss or fixer.

It was found that these tainted monies were used for purposes other than simply political contributions. In many instances they were the source of funds that were used for payoffs to foreign government officials, sometimes made directly, other times through shell corporations abroad, in other instances to ostensible agents but with a clear knowledge that their ultimate destination was a government official or someone else in a situation to procure official favor. We were staggered as each report seemed to outstrip the last in magnitude. First, a few hundred thousand dollars; then a few million; then over thirty million; and now we have learned of political contributions by one American corporation which in one country alone exceeded \$46 million over a period of years. Almost daily, either the Securities and Exchange Commission or Senator Church adds a new internationally-known corporate name to the list of those who have engaged in questionable conduct. While none of us wants to paint with an unduly wide brush, the suspicion grows that this disease may indeed be more widespread than any of us dared to suspect. Thus another of our illusions, another of our devoutly held beliefs, another of the lifelines that safeguarded our confidence in the so-called American system has been savagely and tragically destroyed.

I think that confidence in our institutions and in the people who lead them is one of the essential cements of our society. In the political arena, as a consequence of the accession to the presidency of a man of indisputable honesty and integrity, and as a consequence of legislation designed to curb the possible influence of money upon the outcome of federal elections, the bricks of confidence in our political life are once more being mortared securely in place and we are once again able, hopefully, to withstand the ordinary shocks and strains of national existence.

Our confidence in our business institutions and in its leadership is still unfortunately in the process of disintegration; how long that process may continue is a

problem for all of us. Once a genie like this is out of the bottle, there is no stuffing it back in. The play must go its course and something approximating the full dimension of the evil must be limned. The fury that has been unleashed must spend itself, and, in time, it will.

While the tragedy is unfolding, I think all of us who are in positions to influence the manner of unfolding should exercise our responsibility and our authority in the most cautious way. When we confront this sort of national crisis, the temptation is to use the strongest catharsis, to expose every nitpick and every detail of every peccadillo of which wrongdoers have been guilty. To some extent perhaps this is sort of a national self-purging, an ordeal that we think we must undergo to be sure that any guilt which may attach to us as citizens for the conduct of our fellow citizens is destroyed. Perhaps to some extent it is a desire to be sure that not a single cell remains from which a new growth of evil might come. Like a conscientious cancer surgeon, we want to assure to the fullest extent we can, that never again will we endure this agony.

The danger, of course, is that in the process of our self-inflicted surgery, we may destroy much healthy tissue. We must not allow our sense of rage at wrongdoing to blind us to the other realities and dimensions of the problems. I do not believe this must happen in order to root out the evil.

The Commission's role in all of this is not that of an avenging God seeking to conquer the malefactors. We are not the enforcers of the federal laws with regard to corruption in politics; we are not the enforcers of such codes as exist abroad with regard to the corruption of public officials; we are not the policemen throughout the world of business morality or even legality. Basically and simply, the Commission is an agency that seeks to enforce the federal securities laws. Those laws relate mainly to the disclosure of information material to investors when they are making decisions to buy, hold or sell securities and when as shareholders they exercise their voting rights. Consequently our focus at the Commission must unerringly be on the question of how all

this, and the information related to it, impacts the investor. To what extent must an investor know, to make the choices I indicate, the extent to which his management has used corporate funds to favor candidates selected by the top officials; to what extent must an investor know that his funds have been squirreled out of the accountability process, sequestered in clandestine pools and then directed into illicit channels?

The obvious temptation is to say: make them tell all – every last jot and tittle must be exposed to the sunlight. The unfortunate by-product of this course would be harm to many people. In some instances, large investments overseas might be jeopardized with consequent loss ultimately falling on the shareholders of the enterprise; in other cases, legitimate business opportunities might be lost; in others, even lives might be threatened.

The Commission is at the moment seeking a means by which the legitimate interests of investors can be accommodated to the fullest extent possible consistent with these other concerns. I do not think such an accommodation is fanciful or impossible or improper. It seems to me that an investor can be told all that he really needs in assessing an investment or a proposal without compelling disclosure of information that may have the unfortunate impacts I have suggested. If the Commission can develop such a mode of disclosure, then I think corporations may begin cleaning out their houses voluntarily and without the direct impetus of a Commission investigation or a subpoena from Senator Church's subcommittee.

Under such a program companies not under investigation by us, but which believed they had followed practices similar to those which have been the subject of our enforcement proceedings, would, after notifying us, commence internally, with the assistance of outside directors, auditors and counsel, an inquiry similar to those conducted within Ashland Oil and Northrop. At the conclusion of the inquiry they would inform us of its outcome and the disclosure they proposed to make with regard to any past conduct. Such disclosures, which would be cleared with the Commission's staff,

might reasonably be framed to disclose the approximate extent to which any significant part of the company's business had been secured with or depended upon questionable payments overseas and how disclosure or discontinuance of payments might impact such business, but the company might omit information such as recipients, countries where payments were made and other damaging details which would relate only peripherally to the interests of investors. Of course, practical problem will be encountered in specific cases in developing disclosures that tell that which investors need but not that which would needlessly harm or endanger economic interests abroad. I am confident that the combined ingenuity of businessmen, their auditors and counsel, and our staff can solve these problems.

Obviously we would necessarily have to retain the right, if we thought a management was less than candid in disclosing the extent of its past misconduct, or if other circumstances necessitated, to undertake our own investigation and enforcement proceedings.

It should be noted that this approach has some elements in common with what we are already doing. An integral part of our enforcement procedures in these matters to date has been the provision in our settlement agreements for essentially internal investigations of companies, either by means of committees of the board, plus in some instances additional people, or special counsel. Thus far this method of completing the complicated chore of unraveling the skein of misconduct has been quite successful.

As for the future, we are seeking to develop guidelines for disclosure so that before the company undertakes a course of action either at home or abroad, it will know the extent to which it might have to be disclosed under our laws.

We are anxious that there be provided a means by which apprehensive managements, wondering when the Commission's attention will turn to them, can anticipate such action and work constructively with us to serve the interests of future investors as well as their present shareholders through carefully constructed, responsible

disclosure. Through this means we would hope to wash down the decks, provide the cleansing that must precede or accompany the next step – the restoration of American confidence in its businessmen.

American confidence in American business has been constantly eroding for years, notwithstanding the earnest efforts of industry's public relations experts to stem the erosion. This is evident in repeated polls; the Louis Harris organization not long ago reported that the number of Americans who said they had a "great deal of confidence" in business leaders had dropped from 55% to 27% between 1966 and 1973! It is fueled by the swelling number of exposes concerning corporate conduct, not only with respect to political contributions and misconduct overseas, but as well by the Federal Energy Administrations's frequent allegations against major oil companies that they over-charged, the stories of industry lobbying against clearly justified safety and environmental restrictions, and numberless other instances in which the public with good reason has been caused to doubt industry's dedication to the most urgent concerns of the American public. Incidentally, where were the public relations men when several oil companies decided to raise gasoline prices on the eve of the Fourth of July weekend when annually Americans take to the roads in overwhelming numbers?

The time in my estimation is long past due when American businessmen must face up more effectively than they have to this problem of waning American confidence in them and their efforts. It is apparent that rousing speeches about the benefits American business has bestowed, reminders of the unparalleled American standard of living made possible by American business, condemnations of government interference with free enterprise, can no longer avail. The actualities are too grave, the expectations of Americans too shattered, to rely simply on more of the same to bring back confidence in American business and its leadership.

What is needed is a new approach, one which some businessmen are recognizing as an essential endeavor if business is to be restored to eminence in our society.

Businessmen, who increasingly have sought the accolade of “professional,” must develop within their community a means of developing and enforcing a code of responsibility. It may well be, given the breadth of questionable conduct being exposed of late, that many of those involved in establishing such a venture would be repentant sinners, but perhaps they may become, given their experiences, among the most dedicated supporters of the endeavor.

Businessmen have been singularly slow to raise their voices in criticism of the conduct of their fellow businessmen, conduct which inevitably hurts all businessmen. Not surprisingly in the face of such silence Americans assume that the misdeeds are either condoned or are simply representative of practices universal in the business community. Such conclusions are unfair to the mass of businessmen who, despite the recent exposes, I am convinced are much more comfortable hewing to a narrow line of right than engaging in illegal payoffs, secreting caches of money, or bribing foreign officials.

The business community should vigorously undertake, perhaps through some existing entity, but better through a new privately organized agency, the articulation of standards of conduct for business and businessmen. The areas such a code might embrace are almost without number, but certainly such a code should contain strong condemnations of interference with political processes abroad, the establishment of secret funds outside the normal channels of accountability, the flaunting of American laws concerning election contributions. But more important than the formulation of the code is the establishment of procedures through which violations can be dealt with. Business cannot, despite its aspirations, be totally like the established professions: a lawyer found guilty of violating the bar’s ethical code can be denied the right to appear in court or advise clients; a doctor who similarly errs can be denied the right to treat patients – in short, they may be denied the opportunity to make a living in their profession. But a businessman can hardly be denied the right to “practice” business and it is unlikely that

drumming him out of the National Association of Manufacturers will be an unbearable penalty.

I would think that as a minimum a businessman whose conduct transgressed the code should be publicly condemned by a privately organized group of national leaders including, in addition to business leaders, other men and women of repute and standing. It may well be that such a condemnation will cause some businessmen and customers, in a manner free of any taint of boycott or organized action, to turn their business favor elsewhere until there is assurance that the condemned practice has been totally abandoned.

Business constantly complains of the intrusion of government in its affairs. I can think of no better antidote to this tendency than strong action by businessmen to prove to legislators and regulators that they are truly concerned with the conduct of their fellow businessmen and that they are willing to move vigorously to identify those who do not share the highest ideals of American business. I would not suggest that federal regulation will wither under such a sun, but I think that the words of business will sound with a new sincerity if spoken by professionals wedded to a new business morality strenuously enforced in some meaningful way.

There is no more urgent task before responsible Americans in this bicentennial year than the restoration of our fellow citizens' confidence in American institutions and American leadership in every field of endeavor. Those who would go about their business heedless of this crisis of confidence deserves nothing but our contempt and condemnation; those who respond to this urgent need merit the name "patriot" and are truly worthy to celebrate this nation's bicentennial. Businessmen, government officials, all of us who share responsibility in this society can contribute nothing more meaningful to generations to come than the gift of restored confidence in our nation, its institutions and its leaders. But such confidence must be earned and merited. I would hope that our

business leadership will quickly erase the cancers in their midst and move swiftly and surely to a new day of responsibility and service.