THE CHAIRMAN OF THE
COUNCIL OF ECONOMIC ADVISERS
WASHINGTON

June 17, 1983

MEMORANDUM FOR SUBCOMMITTEE ON GOALS AND MISSIONS

FROM: William Poole W.P.

SUBJECT: Draft Report

Attached is a copy of my first pass at a Report for our subcommittee. Please return comments (handwritten in margins o.k.) no later than close of business Wednesday June 22. I will be leaving for a vacation at the end of the day on June 24 and so must finish the report before then.

TEXTNAME: TaskForce (R)P: (Report) 01

June 14, 1983

DRAFT

MEMORANDUM FOR THE TASK GROUP ON REGULATION OF FINANCIAL SERVICES

FROM: William Poole

Subject: Report of the Subcommittee on Goals and Missions

This Report is divided into two major sections. In the first, the goals of financial services regulation are discussed. In the second, the missions of the various Federal regulatory agencies are outlined.

I. Goals of Regulation of Financial Services

To discuss the goals of financial services regulation it is necessary first to define a frame of reference. Regulation changes the way unconstrained markets work. It is natural, therefore, to define the frame of reference in terms of how unregulated financial markets work. That standard enables us to examine what regulation is meant to accomplish.
Another reason to analyze regulation against the standard of the behavior of unconstrained markets is that the organization of economic activity through competitive unregulated markets is generally accepted as leading to optimal results. Regulation is justified when the behavior of unconstrained markets is unsatisfactory. In the United States the burden of proof rests with those who advocate regulation rather than with those who advocate free markets. This is probably true except in the case of consumer protection in the U. S.

The behavior of an "ideal" competitive market provides the standard against which we judge the effectiveness of regulation and within which we examine conflicts among regulatory goals. To be justified, regulation must alter and improve the behavior of unconstrained financial markets. Regulation that interferes with desirable market processes should be eliminated unless it yields clear benefits. Regulation that duplicates the results of market processes is redundant and should be eliminated.

The free market standard underlying the analysis in this report is the only natural frame of reference for examining regulatory issues. There is a powerful body of economic theory and evidence relevant to forming judgments on regulatory issues, and this body of knowledge ought to provide the basic background for regulatory decisions. In general, the economic theory justifying regulation relies on the concept of "market failure". In this regard it is useful to divide regulatory goals into two basic groups. One group involves goals intended to correct market imperfections. That is, the desired outcome is a regulated market that behaves more like the perfect market of economic theory than would an unregulated market. For this group of goals the arguments concern the performance of unrestrained financial markets -- how closely they approximate perfect markets -- and whether regulatory interventions in fact improve the functioning of these markets.

The second group of regulatory goals includes those that involve changing the behavior of markets as compared to the behavior of a perfect market. That is, the standard of

the perfect market of economic theory is rejected in certain respects. The issues raised in this regard are usually those of stability, equity, and risk rather than of efficiency.

Historically, most financial regulation arose from perceived problems with market outcomes, especially following crises or severe problems in financial markets. If regulation arose in response to particular historical episodes--for example, the financial problems during the Great Depressions--it is obviously important to examine whether the market conditions that gave rise to regulation still exist and, consequently, whether the need for particular regulatory interventions still exists.

One final point justifying emphasis on the behavior of the unregulated market as a frame of reference is that market forces constrain regulators in a powerful way. The financial markets in the United States are extraordinarily competitive and innovative. Regulation may in some cases do much more to change the forms than the facts of market behavior. Where regulation imposes costs on private firms regulatory avoidance is to be expected. There is no point in arguing the merits of a particular regulation if market forces will ensure the demise of the regulation in due time in any event. This issue is explored more fully below.

There is a presentational problem to an examination of the goals of financial regulation. The issues are intertwined and interconnected. If we think of the various regulatory goals as being represented as points on the circumference of a circle,

there are lines across the circle, connecting all the points with the other points in a tangled web. The order in which the issues are taken up below does not reflect any sense of priority but rather an attempt to present the issues in the clearest possible way considering the interconnections among them.

Stability in the Regulatory Environment

Many, though not all, regulations impose costs on regulated firms and their customers. Where regulation imposes costs there is a market incentive to avoid the costs by avoiding the regulations. Regulatory avoidance--an inevitable and predictable result of costly regulation--is an especially important problem in the financial area because of the fungibility of money. With market avoidance, the effectiveness of regulation declines over time.

One governmental response to avoidance may be the spread of regulation to new firms and new markets. However, the spread of regulation increases costs and frequently has undesirable side effects. Moreover, the regulatory avoidance behavior is simply displaced to new areas. All regulation, and especially financial regulation, risks a never ending process of regulatory response followed by market avoidance. Such a situation is not a stable one, and involves constantly changing rules and unnecessary uncertainties in the market place.

Where the goals of regulation are deemed important, but market avoidance a significant factor, there is only one

possible way to maintain a stable regulatory environment and to achieve the substantive goals of regulation. Regulated financial firms must be provided with offsets to the costs imposed on them by regulation. For example, tax advantages for regulated firms can offset the cost of regulation and prevent market forces from breaking down the regulations.

Consumer Protection

Most aspects of regulation in the financial markets involve consumer protection issues of one kind or another. In this section the topic will be consumer protection relatively narrowly conceived.

A traditional function of government is to enforce contracts and to attack fraudulent representations. Many of the activities of Federal regulatory agencies involve pursuit of these goals.

Some financial regulation is rather similar to the maintenance of weights and measures standards. The definitions of a "deposit" and of a "broker" are controlled by regulation and licensure. The maintenance of standards makes market activity more predictable and efficient. The enforcement of standards reduces the opportunity for consumers to be misled by false claims.

While the maintenance of standards is useful in encouraging orderly market processes, there must always be concern that innovative products and services may be excluded from the market by rigid regulatory requirements. Licensure

of individuals and chartering of institutions should maintain standards but not limit entry.

An important part of consumer protection policy in the United States has been disclosure requirements. Disclosure is not per se a goal of financial regulatory policy, but rather an important part of the goal of consumer protection. Following the general principle of attempting to make markets more perfect, it is widely assumed that full disclosure--in the marketing of securities and in credit (truth-in-lending--should be required by regulation. But with regard to specific borrowing and lending decision. The judgment of investors and borrowers is to be trusted rather than the judgment of government regulators themselves, provided that the required information base is available.

In pursuing the goal of consumer protection, the importance of market processes themselves should not be underestimated. Required disclosure always run the danger of producing masses of data rather than true information.
In the absence of regulation the demand for information can be expressed in investors and consumers' choices of firms with which to deal. Private firms providing financial information, investment advice, and company rating hae long played an important role in U.S. financial market. In an unregulated competitive market the absence of a particular kind of information may reflect the lack of demand for the information rather than the lack of supply. Requiring release of data through regulation may in some cases add to costs without producing information of particular value to consumers.

Just as competitive markets frequently respond to the demand for information without the necessity of regulatory requirements, so also do competitive markets provide a substantial degree of consumer protection from fraudulent and misleading practices. Firms expecting to remain in business have a great incentive to maintain reputations for fair and honest dealing.

In examining consumer protection issues, deposit insurance deserves special attention. An important function of deposit insurance is to provide for the absolute safety, in nominal value, of the funds of relatively small depositors. A careful analysis of this issue makes clear that the regulatory goal cannot be the protection of families' wealth per se; to provide such protection regulators would be required to run families' finances in entirety. It is not the function of government to attempt to prevent individuals from squandering their resources; if it were governments would not be operating and advertising lotteries.

What deposit insurance can do is to provide for the existence of safe assets for individuals who want to hold such assets. But there should be no compulsion on individuals to hold insured assets. Indeed, regulators should be aware that if regulatory costs reduce the returns available on insured deposits there will be an incentive for individuals to hold non-insured assets.

In sum, the goal of consumer protection is an important one for the financial regulatory agencies. The general

approach followed--to prevent fraud and to provide consumers with the means to make wise financial decisions--is sound. Disclosure provides information; insurance provides a safe asset; suitability requirements prevent brokers and dealers from encouraging individuals to buy investments unsuited to their financial position but do not prevent brokers from taking orders from individuals who insist on buying such investments. Nevertheless, specific regulations must be judged against the background of market mechanisms that also provide consumer protection. Excessive regulation, though intended to promote consumer protection, may have a perverse effect. Regulation may increase costs, slow down the speed with which transactions can be made, and reduce the pace of innovation. The users of financial services are then not being protected, but rather burdened.

Maintenance and Encouragement of Competition

Competitive markets are not desired per se; rather, it is generally agreed that the organization of economic behavior through competitive markets provides the widest possible range of goods and services, produced efficiently. Competitive markets are ordinarily progressive and innovative. And, competitive markets limit the economic and political power of particular firms that so often accompanies the concentration of economic power in the hands of a few firms or of government agencies.

From the point of view of regulatory design it is nevertheless best to think of competition per se as being a goal of regulation. The workings of the invisible hand are all too frequently misunderstood precisely because they are invisible. To some, competitive markets seem chaotic and inefficient. To say that the goal of regulation is "efficiency" may invite the restriction of competition in the name of economies of scale, "orderly" markets, or whatever. It is better, therefore, that competition itself be a goal of regulation, and to place the burden of proof on those who would restrict competition.

There is another reason for emphasizing the goal of competition. Markets are meant to serve people, and the best judges of what people want are the individual users of financial services. Only under competitive organization can the principle of consumer sovereignity be given full scope. In the absence of other considerations, consumers should be free to choose their own consumption patterns, which can differ from one individual to the next.

Subsidiary to the goal of maintaining and encouraging competition is the goal of maintaining entry as open as possible. Also, anti-trust policy may be used to prevent collusive practices and excessive concentration through mergers.

The principle of competitive equity--the so-called "level playing field"--is essential to maintain a business envirnment in which the government treats firms in a fair and equitable

manner. It is also an important aspect of the goal of promoting competition. Different types of financial institutions compete, to a greater or lesser extent, with each other in various financial markets. For all of the different types of institutions to prosper it is necessary to maintain at least a rough parity in competitive conditions. Parity in competitive conditions does not require that all financial institutions have the same powers; those with restricted powers must be compensated in some fashion--perhaps through the tax law--so that they are not at a competitive disadvantage.

When one class of institutions is placed at a competitive disadvantage through regulation, the goals of regulation cannot be achieved. Regulatory avoidance will break down the effectiveness of regulation. The degree of effective competition in the marketplace is also reduced.

Finally, the organization of the regulatory system itself should involve considerations of promoting competition. The danger of concentrated financial regulatory authority has long been recognized in the United States. The maintenance of a dual banking system and divided Federal responsibilities provides a system of checks and balances, thus reducing the possibilities of excessive regulation.

Some decry the fact that financial institutions can, to some extent, "shop" for their regulators by changing their charters. This shopping is merely the system of checks and balances within government at work. It is, of course, not

always wise to permit such shopping; but nor is it always necessary to eliminate it. The obvious cost of overlapping jurisdictions and conflicting authorities must be traded against the avoidance of excessive regulatory power due to concentration of regulatory authority.

Maintaining and Improving the Stability of the Financial System

In the United States there has been a high correlation between financial distress and "bad times"; bank failures and other financial problems during periods of depressed economic activity have over the years led to more extensive regulatory control over financial institutions. Whether or not past extensions of regulation reflected sound analyses of problems in financial markets, without question the overriding goal of financial regulation must be to stabilize the financial system and the economy as a whole.

Sharp changes in economic conditions place generalized pressures on financial institutions. Rising inflation and rising interest rates in the late 1970s produced particular problems for the thrift industry. Weak economic activity and rising unemployment is typically accompanied by rising bankruptcies and loan defaults, which weaken the balance sheets of many financial institutions.

Since both inflation and recession place strains on financial institutions, one important consideration in financial regulation is the maintenance of stable economic conditions generally. Successful monetary and fiscal policies are obviously the main ingredients to overall economic

stability, but financial regulation also plays a role. In the 1970s market avoidance of financial regulations--especially Regulation Q--produced a degree of confusion in the measurement of the monetary aggregates, thereby complicating the task of monetary policy and increasing the probability of policy errors.

One approach to attempt to avoid these stabilization policy difficulties would be to maintain much tighter regulation over institutions issuing deposits and near-monies through strict regulatory control over the definitions of deposits and the issuance of them by various financial institutions. The problem with this approach is that it is in conflict with the goal of fostering competitive markets. Moreover, this expansive regulatory approach may not even be feasible given the constraints within which the financial system and financial policy operate. For example, a long-standing policy has been the promotion of highly competitive long-term capital markets. It is probably not possible to maintain this attitude toward the capital markets and at the same time to adopt to much tighter regulation over depository institutions and the close money substitutes that exist in the short-term money markets.

The conclusion from this line of argument is that it is important that regulation in the depository end of the market not be such as to provide incentives for widespread regulatory avoidance that will muddy the definition and measurement of the monetary aggregates. The maintenance of competitive equity is

important. Regulatory costs born by regulated firms should be offset by tax advantages or other methods.

For purposes of the management of domestic monetary policy, regulation should provide an information base that is as complete as possible. The monetary authorities need information on financial flows and credit terms on a timely and comprehensive basis. While such information is frequently a by-product of regulatory activities, its importance should not be overlooked.

No matter how successful the government may be in maintaining economic stability, from time to time there will be disturbances in the financial markets that must be managed and contained. Regulation should serve to isolate financial disturbances and prevent them from spreading to other firms not directly involved. The classic problem, of course, is that of bank runs caused by irrational fears of bank failures. Deposit insurance is the main protection against irrational fears on the part of small depositors, who may not have either the expertise to obtain full information or the incentive to do so because of the relatively small amounts of funds involved.

Deposit insurance, however, does not prevent large depositors, who are mostly uninsured, from tranferring funds out of troubled financial institutions. One solution, attractive on the surface, would be the extension of deposit insurance to all deposits regardless of size. But this solution immediately raises other problems, for it means that the government would be transferring risks from more risky to less

risky institutions, or to taxpayers in general. There ought not to be an incentive for risks that ought to be born by individual investors large in the securities markets to be transferred to others. For example firms now issuing commercial paper ought not to be given an incentive to take out bank loans merely because the loans are supported by 100 percent insured deposits. Market assessment of risks ought to continue to determine interest rate differentials in the commercial paper and bank commercial loan markets. Otherwise, regulators will have to make judgments on risks and either charge differential insurance premiums or control bank portfolios more directly. In the design of deposit insurance there is, in short, an inherent tension between the goal of financial stability and the goal of efficient competitive markets.

Several principles are helpful in thinking through the design of regulations to foster stability while maintaining efficient competitive markets. Above all, the maintenance of stability requires the avoidance of generalized financial panics. The goal of stability is not, therefore, inconsistent with the failure of individual financial institutions with accompanying losses to individual depositors. Efficiency requires that stockholders and managers of financial institutions, and probably large depositors also, be at risk when financial institutions fail. The greater the risk of loss from bad decisions the greater the incentive for good management of financial institutions.

Efficiency requires that decisions be well-informed. If depositors transfer funds for reasons largely unrelated to the efficiency with which a financial institution is managed, then those movements of funds do not serve to reward efficiency. As noted before, small depositors are particularly likely to move funds in response to the irrational fears that arise during financial panics. Such transfers of funds may have nothing to do with the efficiency of the financial institutions from which funds are moved or to which funds are moved. For this reason, deposit insurance for relatively small accounts serves the purpose of improving stability without impairing economic efficiency.

There is, of course, no sharp dividing line between "small" and "large" deposits. There is a continuum along which the balance of considerations shifts such that at some point it becomes reasonable to set a deposit limit for purposes of deposit insurance. Also, as noted in the section on consumer protection, deposit insurance for relatively small accounts serves the additional function of providing a default free asset for relatively small savers.

Minimization of Direct Costs of Regulation

The benefits of regulation--the fostering of competitive conditions, the maintenance of financial and economic stability, etc.--must be set against the cost of regulation. These costs include costs to taxpayers, costs to firms as they comply with regulations, and costs to users of financial services who receive lower returns than would otherwise be the

case. The issue of minimization of the costs of regulation arises in the area of financial regulation as well as all others areas where regulation occurs.

The costs of regulation can be reduced by reducing the amount of regulation and by pursuing regulatory objectives through more efficient techniques. Generally, opportunities exist in most areas to pursue regulatory objectives through a greater reliance on market mechanisms. The substitution of prices and charges for regulatory prescriptions is frequently cost effective. Some activities might be better handled by the market directly. For example, the insurance of some financial institutions is already handled by private insurance companies and/or state insurance companies rather than by Federal insurance agencies. Although the question of who insures the insurers naturally arises, it may still be efficient to design a policy to provide a Federal backstop for private and state insurance companies rather than for the Federal Government to provide the basic insurance directly.

With respect to the administrative costs of financial regulation, an issue that has arisen repeatedly over the years concerns the organization of Federal regulatory agencies into an apparently conflicting and overlaping structure. To many, the organization chart looks messy. Many respondents find themselves burdened with multiple regulation that seems excessively costly. Reorganization of the Federal regulatory agencies deserves careful attention.

Although the problems raised by conflicting and overlapping regulatory jurisdictions are no doubt real, reorganization of the Federal regulatory structure may conflict with the goal of encouraging a competitive organization of the financial industry. Multiple regulatory agencies have fostered a diverse and innovative financial system. Moreover, the present structure regulatory reflects a long-standing policy of providing for a system of checks and balances within government. The "logical" organization of regulation into a unitary structure may improve the efficiency of regulation in the sense of eliminating duplicate forms and conflicting jurisdictions, but at the same time may reduce the diversity of the financial system and its competitive, innovative nature. The organization of governmental agencies should not be judged by the standards of business organization; businesses are constrained by competitive market pressures in a way that governments are not.

Avoidance of Distortions in Credit Allocations

Financial regulation should assure open access by all to credit on a nondiscrimintary basis. This goal is generally accepted, although there are considerable differences of opinion as to what specific regulatory actions in fact promote open, non-discriminatory access to credit.

Some have felt that special regulatory attention should be given to correcting various institutional barriers to credit for small business, homeowners, state and local governments,

and perhaps others. But the goal of nondiscriminatry access to credit is not at all the same as the goal sought by many--the goal of special access. Experience suggests that attempts to use regulation to provide special access to credit for particular sectors is undesirable and, ordinarily, unsuccessful in the long run. Attempts to maintain special access through regulation almost always involve the creation of regulatory costs for particular institutions in the form of lower than average rates of return. Lower rates of return cannot be retained indefinitely through regulatory constraints; funds simply move elsewhere. Thus, efforts to achieve special access, or lower credit costs, should not be pursued through regulation but rather through tax and expenditure provisions that direct funds to the particular institutions and sectors involved.

II. Agency Missions - Summary

(Summary paragraph to be added. Attached FHLBB statement received late and has not been incorporated in text as yet.)

Commodity Futures Trading Commission

TO REGULATE FUTURES TRADING IN A BROAD RANGE OF PRODUCTS AND INSTRUMENTS UNDER A UNIFORM NATIONAL REGULATORY SYSTEM WHILE ENSURING THAT MARKET ACTIVITIES ARE CONDUCTED IN A FAIR AND ORDERLY MANNER.

The CFTC has followed a functional approach to the regulation of all futures trading under which the same basic economic and legal standards are applied to futures contracts for all types of products (e.g. farm commodities, precious metals, energy resources and financial instruments) so that a single contract market can, for example, trade futures on grain and a stock index under the same regulatory structure. The economic purpose of futures as commercial hedging and price basing instruments remains the centerpiece of CFTC regulation.

Fair and orderly market activities are assured by statutory and regulatory provisions for (1) the licensing of contract markets to trade only those futures contracts providing the described economic services; (2) the registration of industry professionals who deal with the public; (3)

reporting and market surveillance programs designed to prevent excessive speculation and unwarranted price movements; (4) industry self-regulation by the contract markets and designated futures associations; (5) proscriptions against manipulation, fraud and other market abuses; and (6) a wide array of enforcement tools.

The resulting regulatory structure reflects a balance between industry self-regulation by the exchanges and the National Futures Association, and governmental oversight by the CFTC, to ensure adequate customer protection as well as market integrity.

Comptroller of the Currency

1. TO PROMOTE AND ASSURE THE SAFETY AND SOUNDNESS, WHILE REQUIRING A HIGH LEVEL OF COMPLIANCE WITH LAW, OF THE NATIONAL BANKING COMPONENT OF THE FINANCIAL SYSTEM.

The regulatory philosophy of the OCC is that a relatively free competitive marketplace, both domestic and international, offers the best assurance that the financial system will make available to the public the widest possible array of financial services. A corollary is that such a marketplace is the most efficient allocator of financial resources.

The principal statutory role of the OCC is the supervision of the national banking system which is a component of the financial services industry and the capital market system. While supervision includes examination of and selective intervention at banks to accomplish certain OCC goals, it also encompasses a wide variety of other activities whose purpose is to ensure that national banks remain a vital part of the financial system.

2. TO PROMOTE THE COMPETITIVENESS, EFFICIENCY, INTEGRITY AND STABILITY OF THE FINANCIAL SERVICES MARKETPLACE.

This mission involves a balancing of often conflicting concerns and reflects the conviction that, given a reasonably stable marketplace, the welfare of the users of financial services is the primary concern. While the prime interest is the development of a superior financial services system offering lower costs with acceptable market risks, OCC strives to improve the competitive capability of the national banking system.

In addition, this mission reflects the belief that banks have an ethical as well as legal repsonsibility to provide financial services without prejudice and on a fair basis to all customers.

Federal Deposit Insurance Corporation

TO FOSTER STRENGTH AND RELIABILITY IN THE FINANCIAL SYSTEM BY INSURING DEPOSITS AND THROUGH AN ASSOCIATED PROGRAM OF SUPERVISION AND ENFORCEMENT DESIGNED TO MAINTAIN AN ACCEPTABLY LOW LEVEL OF BANK FAILURES.

Ancillary to this mission is the function of acting as receiver of failed national and state chartered banks.

Accomplishment of this mission contains other essential statutory provisions relating to bank financial reporting, creation of deposit insurance banks, payment of insured deposits, assistance to insured banks, extraordinary acquisitions and the authority to borrow from the Treasury.

Federal Reserve

1. TO PROMOTE A STABLE AND SMOOTHLY FUNCTIONING FINANCIAL SYSTEM, ONE THAT IS CAPABLE OF MEETING THE FINANCIAL REQUIREMENTS OF THE NATION UNDER A VARIETY OF CIRCUMSTANCES.

This mission reflects the fact that Congress and the Nation often look to the Federal reserve for guidance or action on various aspects of credit and money markets, especially when activities in these markets may have the potential to affect the overall economy.

This mission involves a variety of actions: First, to affect the price and aggregate volume of money and credit in order to attain the Nation's goals of price stability and satisfactory economic performance. Second, to implement the broad framework under which banking organizations operate. Third, to exercise the powers necessary to prevent individual institution's difficulties from affecting the soundness of the entire financial system and therefore of the economy. Finally, to perform both oversight and operational roles in the payments mechanism which links the various parts of the economy together.

2. RESPONSIBILITY FOR ENFORCING LAWS INTENDED TO PROMOTE FAIRNESS IN THE DEALINGS OF DEPOSITORY INSTITUTIONS AND OTHER FINANCIAL INSTITUTIONS WITH THE PUBLIC.

<u>National Credit Union Administration</u>

TO SUPERVISE THE SAFE AND SOUND OPERATION OF FEDERALLY CHARTERED CREDIT UNIONS AND TO PROVIDE "LAST RESORT" SHARE INSURANCE OF CREDIT UNION SHARES AS WELL AS AND LIQUIDITY/STABILIZATION LENDING.

Chartering, supervision, examination, insuring, education, and lending activities are combined in this organization which has a multifunctional examiner force and is funded directly by the credit unions. The development of these "specialized"

activities reflects the unique character and financial structure of credit unions and the fact that they are nonprofit cooperative financial institutions which are controlled by their share holding members.

Securities and Exchange Commission

1. TO PROTECT INVESTORS IN THE SECURITIES MARKETS AGAINST FRAUD, OVERREACHING, AND INCOMPETENCE.

2. A COORDINATE GOAL OF THE FEDERAL SECURITIES LAWS IS TO PROMOTE INVESTOR CONFIDENCE IN THE SECURITIES MARKETS IN ORDER TO FOSTER EFFICIENT CAPITAL ALLOCATION AND FACILITATE CAPITAL FORMATION.

Investor protection is both a means to accomplish these two broader goals and an important end in itself.

The Commission pursues these goals in several ways. First, the Commission administers a system of mandatory disclosure by issuers that sell their securities to the public. Second, the Commission establishes a regulatory framework for creating and maintaining fair, orderly and efficient securities markets; in this pursuit, the Commission relies heavily on self-regulation by the securities industry, on the assumption that the industry itself has the resources, motivation, and expertise to establish and maintain high

standards of professional conduct. Third, the Commission provides for the safety and soundness of securities institutions and the system as a whole with its broker-dealer net capital and customer reserve requirements. It also plays a role in providing limited individual protection against broker-dealer insolvency through industry-sponsored insurance for securities customers. Finally, the Commission closely regulates the structure and activities of investment companies.