

ADDENDUM TO THE TESTIMONY  
OF JOHN S.R. SHAD, CHAIRMAN OF THE SEC  
BEFORE THE SUBCOMMITTEE ON SECURITIES  
OF THE SENATE COMMITTEE ON BANKING,  
HOUSING AND URBAN AFFAIRS

MARCH 25, 1983

Chairman D'Amato and Members of the Subcommittee:

The SEC could of course do more with more people and money, but I believe the Commission can maintain its present levels of activity, despite a 6% personnel reduction in fiscal 1984, for the following specific reasons.

The SEC staff is doing an outstanding job at all levels of improving the Commission's productivity. Programs initiated by the Division Directors, the Executive Director and others last year and in progress, are expected to increase the Commission's fiscal 1984 productivity sufficiently to offset a 6% personnel reduction. These programs include the following.

I. Full Disclosure.

Approximately 500 to 1,000 additional companies are expected to become subject to the SEC's reporting requirements in fiscal 1984. However, this increase is expected to be more than offset by the following programs initiated by Director Lee Spencer, John Huber and other senior members of the Corporation Finance Division during the past year and in progress.

A. Computerization.

1. Over 70% of the 9,000 publicly-owned corporations are now being screened by computers which identify possible problem areas and tabulate key ratios and trends.
2. Over 700 additional companies will be programmed this fiscal year and most of the balance are expected to be added within 12 months.
3. Continuing improvements are being made in the selective review process through the use of micro-computers.
4. Conversion from a slow mini-computer to the Commission's upgraded mainframe computer and the establishment of a quality assurance program will enable the Office of Applications and Reports Services to process filings more rapidly and accurately than heretofore.

B. Paperwork Reduction.

During the past year, the Commission's paperwork has been dramatically reduced through:

1. Integration of corporations' registration and reporting requirements. Fifty to one hundred page prospectuses have been reduced to five to ten pages.
2. In response to the Small Business Investment Incentive Act of 1980, the exemption from registration of certain securities offerings (up to \$5 million to other than the general public), as well as the simplification of private placement exemptions have further reduced the Commission's paperwork. Such financings are expected to exceed \$25 billion this year.
3. Also in response to the Small Business Investment Incentive Act, the asset requirement of reporting companies was raised last year from \$1 million to \$3 million, which exempted about 500 companies from the SEC's reporting requirements.
4. The shelf registration rule permits companies to file a single registration statement covering securities they expect to sell from time to time, within two years. Over \$40 billion of shelf offerings have been filed, since the rule was adopted on a temporary basis in May, 1982.

C. Staff Specialization.

Filings are now being reviewed by teams of industry and other specialists, which has materially improved the quality and efficiency of such reviews.

D. Management Techniques.

1. A branch bonus plan, initiated this year, is increasing the quality and quantity of filing reviews per staff year.
2. A procedure review system is presently being implemented to ensure high, uniform standards throughout the Corporation Finance Division.

E. Private Sector Self-Regulation.

Under the aegis of the American Institute of Certified Public Accountants and the oversight of Clarence Sampson, the SEC's Chief Accountant and his staff, the accounting firms that audit over 90% of publicly-owned companies are now on a three-year peer review cycle. These reviews provide better surveillance of accounting practices.

F. Research Forum.

The Commission recently held its first Research Forum at which leading securities analysts recommended improvements in the Commission's disclosure requirements and rulemaking practices. The staff is currently reviewing these recommendations with a view to simplifying and improving disclosures and public releases. Greater future input is also expected from the analysts.

II. Prevention and Suppression of Fraud.

Regulatory simplification places greater emphasis on enforcement activities. However, the following programs, initiated by Director John Fedders, Theodore Levine, Gary Lynch and other senior members of the Enforcement Division last year and in progress, are enhancing the effectiveness of the Commission's enforcement efforts.

A. Visibility.

Violations of the securities laws are inhibited by media reports of apprehensions, settlements and prosecutions. During the past fiscal year, such reports in the Wall Street Journal increased significantly.

B. Computerization.

The computerized Case and Activity Tracking System (CATS) and the Staff Time and Activity Tracking System (STATS) are improving enforcement case and personnel management. They permit senior management to monitor enforcement investigations and litigation throughout the nation, establish and administer priorities and improve productivity by early termination of marginal cases and redeployment of personnel. They also facilitate rapid response to inquiries and coordination with other law enforcement agencies.

C. Private Sector Self-Regulation.

At the Commission's initiative and under its oversight, the exchange and over-the-counter Self-Regulatory Organizations (SROs) are enhancing their electronic intermarket surveillance systems and audit trails, which permit the quick identification of possible manipulation and insider trading activities. The New York Stock Exchange's "Stock Watch" operation has received wide publicity, which inhibits such activities.

D. Coordination.

The Enforcement Division is also improving its effectiveness through closer coordination of the Commission's enforcement attorneys and investigators with the Self-Regulatory Organizations, the state securities regulators, the Justice Department and other domestic and foreign law enforcement agencies.

E. Swiss Accord.

The widely publicized Accord concluded with Switzerland last year removed the haven of the Swiss secrecy laws from those who would trade on inside information. The Swiss banks are sending notices to their clients throughout the world. Such publicity and notices inhibit insider trading.

F. Exemptions.

In accord with the Small Business Investment Incentive Act of 1980, last year the Commission expanded the exemptions of issuers (to exclude companies with less than \$3 million of assets) and of offerings (of less than \$5 million to other than the general public). These measures reduced the universe of potential reporting violations under the Commission's jurisdiction. The foregoing will continue to be subject to antifraud enforcement.

III. Supervision and Regulation of Securities Markets.

Continuing progress on the National Market System and a national clearance and settlement system are consuming significant staff time. However, the following programs initiated by Director Douglas Scarff and other senior members of the Market Regulation Division are enhancing the Commission's productivity.

A. Computerization.

1. New on-line computerized information systems are accelerating the staff's broker-dealer examinations.

2. These include automated data processing systems for analyzing broker-dealer records for churning and other violations.
3. Portable micro-computers are under consideration with a view to increasing the efficiency of the examination process.

B. SECO Program.

1. Over 85% of the nation's registered broker-dealers are being inspected and supervised by Self-Regulatory Organizations, under the oversight of the Market Regulation Division.
2. The remainder (known as SECO firms) are being inspected and supervised directly by the SEC.
3. Legislation proposed by the Commission would require the SECO firms to join a registered national self-regulatory organization, and relieve the Commission of this direct inspection and supervisory responsibility.
4. Since this legislation was proposed, SECO firms which employ over 80% of all SECO registered representatives have voluntarily joined a national self-regulatory organization.

5. This is enabling the Commission to devote greater resources to "for cause" broker-dealer examinations and SRO oversight activities.

C. New Rules and Procedures.

1. At the initiative of the Market Regulation Division, the Commission recently revised the issuer repurchase and underwriter market-making rules.
2. These revisions have reduced the time and expenses of providing interpretations and processing requests for exemptions and other relief.

D. Market Oversight and Surveillance System.

The SROs are enhancing their electronic intermarket surveillance systems and audit trails, under the oversight of the Market Regulation Division. This has enabled the Commission to begin converting its MOSS system to an audit mode.

IV. Public Utility Holding Company Regulation.

Since the basic objective of the Public Utility Holding Company Act - the dismantlement of the multi-tiered holding companies - was accomplished 20 years ago, the Commission has proposed repeal of the Act. In the meantime, Director Aaron Levy and Grant Guthrie of the Corporate Regulation Division, are streamlining the processing of regulated companies applications for approval of their financing, merger, acquisition and other plans. Next year, the Division will computerize this program in order to reduce the labor-intensive review of filings and improve the public's access to such information.

V. Investment Management Regulation.

Significant steps taken by Director Joel Goldberg, Richard Grant, Gerald Osheroff and other senior members of the Investment Management Division are increasing the Division's productivity and effectiveness.

A. Computerization.

1. Investment adviser inspections.

- a. The use of computers is permitting the staff to target those investment advisers which warrant more frequent inspections.
- b. They are also enhancing the staff's ability to predetermine the scope of the procedures to be used during periodic inspections.

2. Investment Companies.

The Division is considering similar techniques which may be employed in investment company inspections during the coming year.

B. Money Market Fund Contraction.

1. Since December 14, 1982, when depository institutions were permitted to offer money market accounts, the money market funds have contracted by \$38 billion (17%) and registrations filed by new money market funds have virtually stopped.
2. This reduction in the Division's workload is being offset to a slight degree by increased interest in equity and other traditional funds.

C. Paperwork Reduction.

1. Codification of Exemptions.

During the past year, the Division proposed rules which would codify exemptive orders previously granted by the Commission. If adopted these will reduce the number of exemption requests.

2. Automatic Effectiveness.

Other steps have been taken to expand the categories of documents submitted by registered entities which can be declared effective without staff review.

D. Self-Regulation.

1. Investment Company Directors.

The Commission has also reduced its paperwork by placing greater responsibilities on investment company directors.

2. Self-Regulatory Organizations.

The Commission has recently solicited public comment on various proposals concerning greater private sector involvement in conducting inspections. One proposal would involve the establishment of an SRO to conduct routine periodic inspections, under the oversight of the Investment Management Division.

E. Regulatory Simplification.

Public comments have also been solicited on concepts which would simplify the structure of investment companies, and reduce their expenses and the Commission's paperwork, but not investor protections.

VI. Legal Services.

The volume of litigation in which the Commission is involved continues to increase. However, efficiencies being introduced by General Counsel Daniel Goelzer, Paul Gonson, Russell Stevenson and other senior members of the Office of the General Counsel are increasing the staff's productivity and reducing its workload.

A. Computerization.

1. Legal Research.

Increasing usage is being made of Lexis, a computerized legal research system, for the preparation of appellate briefs and legal memoranda.

2. Computerized Index.

Commission appellate briefs are being indexed on the computer. Any member of the Commission's staff can rapidly retrieve prior General Counsel briefs on specific topics, without time-consuming research. Consideration is being given to adding General Counsel memoranda to this system.

3. Word Processing.

The Office of the General Counsel is now equipped with modern Lexitron word processing equipment. These memory typewriters have greatly increased the speed and efficiency with which briefs and other legal documents can be prepared.

4. Management Information.

Case and personnel management are being improved through the use of the computerized Case and Activity Tracking System.

B. Reduced Calendar Review.

The counselling group is spending less time reviewing calendar memoranda from other divisions. Its comments are being included in the divisional memoranda, before they are submitted to the Commission.

C. Discretionary Litigation.

1. Bankruptcy.

The Commission's participation in bankruptcy proceedings is discretionary. Only cases with significant potential benefits for investors are being entered.

2. Amicus Participation.

The Commission's amicus curiae participation in federal appellate proceedings is discretionary. The Commission is continuing to participate in leading cases.

VII. Economic and Statistical Research.

The reporting and review requirements of the Regulatory Flexibility and Paperwork Reduction Acts are time-consuming, but Director Jeffrey Davis and other senior members of the Directorate of Economic and Policy Analysis are improving DEPA's productivity through the following programs.

A. Computerization.

New computer systems and programs have greatly enhanced DEPA's ability to collect, compile and analyze statistical data. Additional computer systems and programs are being developed.

B. Broker-Dealer Reports.

Approximately 5% of DEPA's personnel resources are devoted to the compilation, review and editing of data provided in broker-dealer reports. DEPA has begun to shift this program to the SROs.

C. Financings.

Approximately 14% of DEPA's personnel resources are devoted to the collection, compilation, editing, production and dissemination of securities registrations and private placement statistics. Consideration is being given to turning this program over to responsible vendors who would provide the information to the public at a reasonable cost.

D. Economic Staff.

1. The staff economists' ability to conduct timely in-depth analyses is being enhanced through the use of computer systems and programs.
2. Existing data bases of market and economic activity which will eliminate the need to develop such data in-house are also being explored.

VIII. Program Direction.

Productivity innovations now underway, initiated by Executive Director George Kundahl, Kenneth Fogash and the heads of the support offices, will improve administrative services and the efficiency of Divisional and Regional Office programs.

A. Computerization.

1. The Office of Information Systems is expanding the use of software available to user divisions and offices so that they can design their own output reports with little or no assistance required from the ADP staff.
2. The divisions and regional offices are being provided micro-computers to assist in case preparation and litigation.

3. In fiscal 1984, portable micro-computers will improve the capability and efficiency of on-site examinations of regulated entities, standardize inspections and facilitate report writing.
4. The recently automated central personnel data files enhance the Personnel Office's ability to conduct personnel evaluations, determine compliance with OPM directives, and respond to requests for personnel data. Development of software to perform retirement calculations and related services regarding employee benefits will increase the office's productivity.
5. The Comptroller is expanding automation of certain financial management functions which will expedite accounting and budgeting operations.
6. An automated procurement system will permit the Office of Administrative Services to increase the efficiency of tracking purchase orders, modifying contracts, and generating procurement reports.

B. Headquarters Consolidation.

1. Fiscal 1982 results suffered from the usual disruptions of the major move of the Commission's headquarters to a new location.

2. Consolidation of the headquarters in a single building has eliminated the need for time-consuming shuttle services and special messengers between dispersed locations.

C. Training.

The Commission is conducting annual training programs and conferences in each of its five principal program areas to improve the coordination between headquarters and regional staffs, thereby contributing to overall productivity and effectiveness.

D. Printing.

The transfer of the responsibility for printing, collecting and disseminating publications, such as the SEC Docket, SEC News Digest, Commission releases, and the SEC Decisions and Reports, to private vendors has reduced the workload demands on the Commission's printing plant and the Divisions and Offices which previously compiled and edited these materials.

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The foregoing amplifies previous statements (before the Senate and House Appropriations Committees and the House Subcommittee on Telecommunications, Consumer Protection and Finance of the House Committee on Energy and Commerce) as to why I believe the Commission can maintain its present levels of activity, despite a 6% personnel reduction in fiscal 1984. Whatever Congress decides, the other Commissioners, the staff and I will continue to do our best to administer the securities laws effectively.