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THE LEVEL REGULATORY PLAYING FIELD FOR THE SECURITIES MARKETS

Aulana L. Peters
Commissioner

The views expressed herein are those of Commissioner Peters and do not necessarily represent those of the Commission, other Commissioners, or the staff.

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I want to congratulate Robert Googins on his fine summary of the work of the Bush Task Group. It is perhaps particularly appropriate that my remarks are scheduled to follow Bob's since the Commission has been "following up" with commentary on the Task Group's recommendations for quite some time. Following publication of the Task Group's Report, 1/ the Commission endorsed many of the group's recommendations, proposed specific legislation and generally urged Congress to enact its recommendations into law. As you will soon discover, the Commission and in particular this Commissioner are still praising the initiatives of the Bush Task Group, notwithstanding the fact that I have in the past and will today take issue (in a friendly way, of course) with certain of its recommendations.

I would like to focus my remarks on the concept of functional regulation, a concept I wholeheartedly endorse, and analyze two recommendations of the Bush Task Group with that concept in mind. I also would like to comment briefly on the applicability of functional regulation to one area not often associated with the concept. Let me begin by noting generally that I believe the Bush Task Group sought to level the regulatory playing field by simplifying the regulatory structure of the financial services industry through the concept of functional regulation. The concept of functional regulation, simply put,

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1/ Task Group on Regulation of Financial Services, Blueprint for Reform (July 1984) (hereinafter cited as Blueprint for Reform).

is that the activities of commercial entities performing essentially the same services should be subject to the same regulatory framework. 2/ Thus, for example, under the concept of functional regulation, the banking or brokerage activities of nominal insurance companies would not be regulated by state insurance regulators, but instead would be regulated by banking or securities regulators. Of course, the same would be true for banks and brokerage firms offering a full range of financial services, such as insurance.

One Bush Task Group proposal designed to level the regulatory playing field would provide that banks and thrifts issuing securities to the public be subject to the registration requirements of the Securities Act of 1933 and the disclosure and other requirements of the Securities Exchange Act of 1934. 3/ Under the current system, publicly held banks and thrifts are exempt from compliance with the registration and disclosure requirements of the federal securities laws. There is, of course, already some regulation in this area. Each of the four federal bank and thrift regulatory agencies maintains a separate securities division to perform the responsibilities otherwise handled by the SEC for all other public companies.

One obvious regulatory disparity caused by this system involves the securities regulation of banks and thrifts versus bank and thrift holding companies. The disclosure, reporting and

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2/ Letter from Donald T. Regan, Secretary of the Treasury, to John S.R. Shad, Chairman of the SEC (July 12, 1984) (commenting on the SEC's proposed Rule 3b-9).

3/ Blueprint for Reform, supra note 1 (recommendation 5.2).

proxy requirements of publicly held banks and thrifts are administered by the bank agencies and the Federal Home Loan Bank Board, not by the SEC. On the other hand, the SEC has jurisdiction over the disclosure, reporting and proxy requirements of publicly held bank and thrift holding companies, even if the only asset of that holding company is the stock of a bank or thrift. The Bush Task Group proposal would eliminate this disparity and provide more uniform regulation and financial disclosure to investors, and at a lower cost. The changes would reduce costs by eliminating duplication of agency staff needed to establish, interpret and enforce securities disclosure requirements. In my opinion, Congress should act swiftly on this proposal of the Bush Task Group.

While I endorse this proposal, I believe that the Task Group did not go far enough. The Task Group recommended that the Federal Home Loan Bank Board maintain its securities jurisdiction over conversions of thrifts from a mutual to a stock form of organization. 4/ I frankly did not understand the logic of this exclusion, particularly given that the concept of functional regulation was the guiding light of the Bush Task Group. 5/ In my opinion, the process by which thrifts issue

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4/ Id.

5/ The Task Group's report seems to suggest that the conversion of a thrift is a matter "involving the safety and soundness of insured institutions." Id. at 91. However, the Task Group identifies no special regulatory concerns

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stock, whether in a conversion or any other kind of public offering, should be subject to SEC oversight. The principal regulatory concern in a conversion, as in virtually all public offerings, is that the investors receive full disclosure of material facts. The SEC is the one agency expert in ensuring that material facts are disclosed to investors in stock offerings and, therefore, should be the agency having jurisdiction over conversions.

The Bush Task Group also did not address the regulatory disparities that have resulted from increased brokerage activities of banks. Through discount brokerage and other services, banks are today involved in the same types of commercial activities as traditional broker-dealers. Nevertheless, bank brokerage activities have not been subject to SEC jurisdiction, and there are many important rules designed to protect the public investor that do not apply to bank brokerage employees. Examples that readily come to mind are the NASD's fair practice rules.

In order to correct this regulatory disparity, the Commission adopted Rule 3b-9, 6/ which would require banks engaging

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5/ (continued footnote)

involved in such a conversion. Its report argues only that regulatory concerns exist when a thrift issues mortgage-backed securities, and the mortgages backing the securities are a significant portion of the thrift's assets. Id. at 93. Issuance of mortgage-backed securities does, indeed, implicate the safety and soundness of insured institutions, but, in my view, this point is irrelevant to conversions because the newly issued common stock of a thrift would presumably not be a mortgage-backed security.

6/ Securities Exchange Act Release No. 22205 (July 1, 1985).

in certain types of securities activities to register as broker-dealers. Needless to say the banking community did not applaud the Commission's action. The American Bankers Association has sued the SEC, 7/ challenging its authority, to adopt the rule. The SEC, of course, believes it has the authority but as important as that legal question is the fundamental policy issue underlying the rule, namely whether commercial entities performing essentially the same services and selling the same products should be subject to the same regulatory framework. Bringing the brokerage activities of banks within the same type of regulatory structure as other types of participants in the securities industry is necessary in order to protect investors and to level the regulatory playing field.

In sum, despite the generally good work of the Bush Task Group and certain Commission initiatives, I must conclude that we are far from our stated goal of creating a level regulatory playing field for the securities markets. In the long run, however, I see a brighter future. Let me conclude on an upbeat note with some thoughts on that future. In my opinion, one area in which the concept of functional regulation can be profitably pursued is periodic reporting. The SEC's integrated disclosure program has paved the way for EDGAR, presently a pilot program for electronic filing of periodic reports under the Securities Exchange Act. The goal of EDGAR is that one day all registration

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7/ American Bankers Assoc. v. Securities and Exchange Commission, Civil Action, File No. 85-2482 (D.D.C.).

statements, periodic reports and proxy statements will be transmitted electronically to the SEC and stored in computers. Foothigh stacks of paper filings, proofreading at the printer 'till the wee hours, and messengers taking the "red eye" to D.C. will no longer be the dark side of the corporate lawyer's practice. Such phenomena will not exist outside war stories told by pre-computer-era lawyers! In any event, I think the day will soon come when EDGAR spreads beyond the SEC -- insurance companies, banks and thrifts also will someday file their reports electronically with their state and federal regulators.

Electronic filing of reports presents new opportunities to create an inter-disciplinary regulatory framework, based on the concept of functional regulation. It is, I believe, the perfect answer to those who resist application of the "Functional Regulation" concept because of the burden they perceive regulated entities will bear in making multiple filings with several agencies. There is no reason that the concept of incorporation by reference cannot be implemented on an inter-agency basis. Once electronic filing of reports is in place, it should be possible to send parts of reports to various agencies that might require or request them. 8/ For example, a publicly held insurance company might file

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8/ Some steps have already been taken toward incorporation by reference on an inter-agency basis. The SEC, for example, recently proposed a rule that would require publicly held

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electronically and concurrently a report with a state insurance commission and a portion of that report with the SEC. Periodic reports of financial conglomerates can be tailored so that the reports of affiliates can be filed separately with agencies having jurisdiction over particular functions, and then combined for filing with the agency or agencies having jurisdiction over the entire holding company. 9/ The entire process could be "faster than a speeding bullet"; EDGAR and its progeny need take no back seat to Superman.

Take the case of Sears, Roebuck. Sears, as all of you know, owns an insurance company (Allstate) and a broker-dealer (Dean Witter). These affiliates should be able to file reports separately with their respective insurance or securities regulator.

8/ (continued footnote)

property and casualty insurance companies to include, with periodic reports filed with the SEC, portions of reports filed with state insurance commissioners. SEC Securities Act Release No. 33-6559 (Nov. 27, 1984). Currently, §7(c)(1) of the 1934 Act provides that registered clearing agencies, transfer agents and municipal securities dealers that are regulated by banking regulatory agencies shall file copies of their SEC reports with the appropriate banking regulatory agency. In addition, §§17(c)(2) and (3) of the 1934 Act roughly provide for exchanges of information and coordinated action between agencies.

9/ At the SEC at least, the regulations necessary for such a composite reporting system are to some extent in place. The Form 10-K annual report requires registrants to disclose financial information for each of its industry segments. Regulation S-K, Item 101(b) and (c). Of course, those regulations would be amended to allow the incorporation by reference of reports filed with other agencies.

Sears could then assemble those reports, together with reports on other Sears lines of business, when preparing periodic reports to be filed with the SEC for the Sears holding company. This scenario, of course, assumes major advances toward uniformity of regulatory purpose and accounting methods, but I think that electronic filing of reports and incorporation by reference on an interagency basis are worthwhile and practical goals, which someday will be implemented. That is the future I see of functional regulation, and a level regulatory playing field that is both inexpensive and effective.

I thank you for your attention.