TESTIMONY OF THE HONORABLE RAY GARRETT, JR., CHAIRMAN, SECURITIES AND EXCHANGE COMMISSION, BEFORE THE SENATE COMMITTEE ON GOVERNMENT OPERATIONS ON S. 260, 93d CONG., 2d SESS.

October 15, 1974

Mr. Chairman, Members of the Committee: I appreciate this opportunity to present the views of the Securities and Exchange Commission concerning Committee Print Number 3 of S. 260, the so-called "Government in the Sunshine Act."

As you know, a primary task of our agency is to insure appropriate disclosure by those persons to whom the public has entrusted its capital. Accordingly, we are sympathetic to the stated objective of this bill — that is, to require appropriate disclosure by ,those persons to whom the public has entrusted its government. Nevertheless, for reasons I will explain, we believe that the enactment of this bill — specifically, the provisions of Title II — would very seriously, and needlessly, interfere with the effective operation of our agency.

Section 201 of Title II provides generally that "all meetings" of collegial agencies of the government, or any "subdivision thereof authorized to take action on behalf of the agency, "shall be open to the public" and that complete verbatim transcripts of all meetings be made and preserved. While the bill grants a rather limited and cumbersome exemption for certain

enumerated matters, since many matters we consider could, if prematurely published in the press, have serious effects on our securities markets, the bill would require our Commission to consider rather frequently whether to open the discussion of various matters to the public or to disclose the transcripts of various discussions; and would require the agency formally to adopt an explanation for each matter the agency decides it may, and should, withhold.

The procedures proposed in this legislation would, contrary to the public interest, and in a manner detrimental to the interests of investors, tend to

— destroy the flexibility which is the essence of the administrative process;

— impede effective communication among Commission members and between the Commission and its staff, resulting in less well-considered judgments;

— cause wholly unjustifiable administrative delays; and

— create a cloud of uncertainty over agency rules and orders otherwise valid, if the agency should err in determining that a particular meeting may be closed.

We fail to see any substantial public benefit that would result from the enactment of this bill. As Professor Gellhorn has noted in his letter of July 18, 1973, to Senator Chiles, not "every conversation behind closed doors is a threat to public safety and good morals. . . . [T]he risk of inhibiting discussion outweighs the risk of improper discussion."

In this connection, I should emphasize that we are proud of our agency and of the work that we do and have done; we are not reluctant to have our judgments reviewed by the court or our conduct reviewed by the Congress. And, where no substantial adverse effect upon our work is likely to result, we do not hesitate to invite the public to observe the Commission at work. But, we think that there are relatively few categories of matters that are considered or discussed at the meetings of our agency that should not require that discussion, for one reason or another, to be exempt from disclosure.

It seems to us that S. 260 may rest upon certain assumptions concerning what agencies do and how they do it that are not correct. Section 201 of the bill applies only to an agency of the government which "consists of two or more members." This may rest upon the assumption that multi-member agencies in the Executive Branch, or constituted as an independent agency, are closely analogous to the committees of Congress, since the procedures specified in the bill for committees of the Congress are largely carried over to Section 201. While we do have some quasi-legislative functions, however, most of what we do is quite different.

The bill may also implicitly assume that multi-headed agencies are entirely different, and have entirely different functions, from single-member agencies. This is simply not so, as I will point out shortly. For example, the Commission's enforcement responsibilities are essentially the same as those performed by the Attorney General, an Assistant Attorney General or a United States Attorney, particularly where the question is whether or not a

case should be brought in court. And regulatory functions similar to those performed by the Commission are also performed by single-member agencies. National banks, for example, are regulated by the Comptroller of the Currency, who has much the same powers as any other regulatory agency.

The bill, however, would have no application to these single-member agencies notwithstanding the fact that their decisions will often be reached by much the same processes as those of the Commission — the head of the agency will sit down his deputies, associates and staff and they will have same type of discussion among themselves as the members of the Commission have. Yet, there is no thought that the bill be applicable to them. It is hardly conceivable that the President, or the Secretary of the Treasury could not discuss something with members of their staff except in a public meeting.

In order to clarify why we feel so strongly that this proposed legislation should not be adopted, let me emphasize what our agency does and how we do it. The Securities and Exchange Commission is entrusted with broad administrative, regulatory and enforcement responsibilities under the six statutes that comprise the federal securities laws. [FOOTNOTE: The Securities Act of 1933, the Securities Exchange Act of 1934, the Public Utility Holding Company Act of 1935, the Trust Indenture Act of 1939, the Investment Company Act of 1940, and the Investment Advisers Act of 1940. In addition the Commission functions as an advisor to the court in reorganization proceedings under Chapter X of |the Bankruptcy Act.] To

fulfill these responsibilities, the Commission will sometimes meet formally, perhaps to hear the presentation of oral arguments in a quasi-judicial administrative proceeding, or to hear testimony and question witnesses in a quasi-legislative investigative proceeding. Meetings of these types are normally public, and a verbatim transcript is usually made and preserved. Accordingly, if matters of this kind comprised substantially all of our work, S. 260 would have little adverse impact upon our activities.

But, the overwhelming majority of Commission meetings are of a far less formal nature. They are held at least three days a week — sometimes four or five — lasting for many hours at a time — often requiring both morning and afternoon sessions Sometimes they are planned in advance, others are held on very short notice when circumstances require it. At these meetings, the Commission consults directly with its staff and decides a broad range of administrative, regulatory and enforcement questions.

In the course of a typical week, the Commission will almost certainly be required to consider whether to suspend trading in the securities of a dozen or more corporations for a -ten-day period [FOOTNOTE: See Sections 15(c)(5) and 19(a)(4) of the Securities Exchange Act.]; whether to grant authority to its staff to issue subpoenas to investigate apparent violations of law on the part of both individuals and corporate or other business entities [FOOTNOTE: See, *e.g.*, Section 19(b) of the Securities Act, Section 21(b) of the Securities Exchange Act and Section 42(b) of the Investment Company Act.]; whether, based upon the results of completed investigations, to institute

lawsuits [FOOTNOTE: See, *e.g.*, Section 20(b) of the Securities Act, Section 21(e) of the Securities Exchange Act and Section 42(e) of the Investment Company Act.] or administrative [FOOTNOTE: See, *e.g.*, Sections 8(b) and (d) of the Securities Act (refusal or suspension of effectiveness of registration statement), Section 15(b)(5) of the Securities Exchange Act (proceedings against broker-dealers) and Section 8(e) of the Investment Company Act (proceedings against investment companies).] proceedings or refer matters to the Attorney General for criminal prosecution [FOOTNOTE: See, *e.g.*, Section 20(b) of the Securities Act, Section 21(e) of the Securities Exchange Act, and Section 42(e) of the Investment Company Act.]; whether to accept offers of settlement in pending proceedings and actions or to appeal adverse decisions in court actions we have lost; and whether to participate as *amicus curiae* in private actions brought to enforce duties imposed by the federal securities laws.

During the Commission's fiscal year 1973, the Commission suspended trading in the securities of 174 companies — primarily to alert the public to the lack of adequate, accurate and current information about those issuers. [FOOTNOTE: Because the Commission may suspend trading for only ten days at a time, the Commission usually must reconsider each suspension on a number of occasions until appropriate information is available in the marketplace.] During that same year, a total of 472 investigations were opened; 178 injunctive actions were brought; at least 198 administrative proceedings were instituted; and 49 potential criminal cases were referred to the Department of Justice.

In addition to enforcement and related matters, the Commission in a typical week considers a wide variety of regulatory questions concerning, for example, the necessity for new or amended Commission rules prohibiting fraudulent activities or regulating the conduct of national securities exchanges, broker-dealers, investment companies or investment advisers. Or the Commission may have an occasion to review the adequacy of rules that the exchanges or the National Association of Securities Dealers have adopted pursuant to their statutory self-regulatory responsibilities. Often the Commission is given information concerning entities we regulate which, if disclosed before the facts are generally made public, could have an adverse impact on our securities markets.

Interpretative questions are constantly presented concerning even so basic a question as what constitutes a security. And the Commission must consider diverse applications for rules or orders seeking exemptions from various statutory provisions, which the Commission is directed to permit when found to be consistent with statutory aims. This enumeration is by no means exhaustive. There are numerous other matters that we frequently must consider. In this connection, the federal securities acts make over 300 separate provisions for adjudicatory or rulemaking proceedings of one sort or another for which the Commission must take responsibility. [FOOTNOTE: These were set forth in the Commission's response in 1957 to the Executive and Legislative Reorganization Subcommittee of the House Government Operations Committee. See 11D *Survey of Study of Administrative Procedure*

and Practice in the Federal Agencies, 85th cong., 1st Sess. (1957), pp. 1906-1933. While there have been some statutory changes since then, this is a reasonably complete catalog of the types of the Commission's formal determinations.]

Finally, the members of the Commission may simply sit down together informally to discuss a problem or matter for the purpose of exploring it, determining whether the Commission should or should not address itself to the matter and, if it should, how. This might include, for example, whether a staff study or inquiry on a particular matter should be made, whether a rule should be drafted and considered, whether a policy statement should be made, or even whether a Commissioner should mention the matter in a speech. We assume that such discussions would not constitute a "meeting" within the meaning of the bill, but that is not entirely clear since the term "meeting" is nowhere defined.

The exemptive provisions contained in Committee Print 3 of S. 260 reflect an attempt to recognize that enforcement-related matters may be sufficiently sensitive so as to warrant their nondisclosure. Unfortunately, this attempt falls far short of the mark.

For one thing, the specific exemptive provision — Section 201(b)(3) — involves enforcement matters pertaining only to *individuals*, and excludes corporate, or other business, entities, equally entitled to protection from premature disclosure of charges that could prove erroneous. Moreover, it is

not apparent that, under this bill, the Commission could consider the suspension of trading in a security in a non-public meeting, although there might be strong market reaction with possibly harmful effects upon investors if it were publicly known that Commission was considering suspension before a suspension could in fact be ordered. Indeed, there is a risk that persons sitting in on our meetings might attempt to utilize market sensitive information for their own securities transactions.

In addition, the ability of the Commission to rely upon an exemption as to even the limited matters within the purview of Section 201(b)(3) is severely handicapped by the requirement that we first obtain, in writing and in advance of closing any meeting to the public, an opinion from the Attorney General's Office of Legal Counsel that it is appropriate to keep the meeting closed. All the while, important matters affecting the public might have to grind to a halt.

And, under the judicial-review provisions of S. 260, if the Commission thinks it necessary to act non-publicly as to a matter that a court later concludes should have been open, there is a substantial risk that important determinations might be nullified, even though not the slightest hint of impropriety is suggested in connection with our judgment. For this reason also, where the statute is not clear, the Commission would normally have to assume that the exemption from public procedures will not apply, resulting in an unfortunate slow-down of our work in those areas.

In this context, I might add, the traditional presumption of regularity for agency actions would be overturned by the bill, and the burden of proof put on the government to sustain its determination to close a meeting. This will encourage frivolous suits by persons who might not even be affected by our action, since any person desirous of hamstringing otherwise lawful agency action can sue under this provision and require the agency to meet its "burden" of proof, while agency rules and orders might be stayed pending the result.

One of the major basic deficiencies of this bill, is that the exemptive provisions focus solely upon protection of interests outside the government, and reflect no appreciation of the need to protect the integrity of the governmental process itself. The great advantage that is gained through the creation of independent regulatory agencies is that that they can successfully deal with important public issues normally and by use of flexible procedures. This bill, if enacted, would go a long way toward nullifying those advantages, since it would compel public disclosure of all legal and policy discussions, effectively preventing a full and frank exchange of opinions among the Commissioners and with the staff, unless, quite fortuitously, the subject of a particular discussion has been exempted from disclosure.

Perhaps our agency is fortunate in that our five members have a great respect for each other's judgment. The present Commission works as a team, and each of us is normally aware of the types of considerations the others deem most important on numerous types of issues. This, in many instances,

permits a half-dozen words to take the place of a thousand in our internal communications. Were our discussions required to be public, Commission members necessarily would be required to speak for the "record" — for the benefit of the public audience — rather than for the persuasive impact that stronger or more succinct words might have upon their colleagues. Moreover, were the Commission's discussions public, there would be many situations where it would be most difficult to spell out in our discussions certain pertinent arguments because they are premised on facts that might have adverse effects upon the securities markets if those facts were publicly disclosed at that time. In addition, since the bill requires an advance announcement of the subjects to be discussed at its meetings, lobbying pressures upon members of the Commission and its staff would be encouraged.

Of course, the Commission receives written memoranda from its staff on nearly all matters that the Commission considers, and we do not understand this bill to compel disclosure of those memoranda. But, it is our Commission's practice to discuss matters thoroughly with those staff members concerned before attempting to reach a consensus. With some frequency, matters that seem relatively simple to resolve on the basis of written memoranda are shown to have subtle complexities when they are discussed. Our agency has capable staff members who do not hesitate to urge further consideration when they believe that my fellow Commissioners and I do not fully understand a problem, and let us know when they believe we are wrong. As conscientious as these staff members are, however, and as willing as they

may be in private to point the error of our ways, I doubt that very many staff members would wish to make members of the Commission look foolish in a public forum. And, we might not appreciate it if they did. This would leave much unsaid, which might well be the difference in many situations between a good decision on our part, and a bad one.

It may be difficult to explain to those not familiar with the way a commission like ours functions that internal debate and argument are a necessary way of life. Yet, if this proposal is enacted, the press would make principal use of the ability to attend our meetings. Not familiar with our procedures, and anxious to make "news," internal disputes and arguments likely would be played up and exaggerated, with the concomitant result that staff and Commission differences of view would be intensified, and dissension and competition between our staff units would be engendered. Such a result, in our view, would be deleterious to the public and investors.

These are the types of considerations which protect memoranda written by the staff from public disclosure under the Freedom of Information Act. As the members of the Committee no doubt are aware, the fifth exemption from the disclosure requirements of the Freedom of Information Act protects inter-agency and intra-agency memoranda and letters. [FOOTNOTE: 5 U.S.C. 552(b)(5).] The legislative history of this provision is unambiguous that Congress intended to assure that the free flow of ideas would be preserved in written documents that discuss policy matters; and it was recognized that necessary candor would not long survive within government if memoranda

containing policy discussions were publicly disclosed. As the Court of Appeals for the District of Columbia Circuit aptly observed in discussing this exemption:

> "In the Federal Establishment, as in General Motors or any other hierarchical giant, there are enough incentives as it is for playing it safe and listing with the wind; Congress clearly did not propose to add to them the threat of cross-examination in a public tribunal." [FOOTNOTE: *Ackerly v. Ley*, 420 F. 2d 1336, 1341 (C.A.D.C., 1969).]

At the very least, both Commissioners and staff members will be more circumscribed in what they say, and how they say it, if their words are available for public scrutiny, not because of any self-interest or neglect of duties, but merely because of the possibility of misinterpretation, including possible misinterpretation by the press. In our meetings as they are now conducted, one may feel free to take a position for the sake of argument; to explore various possibilities, however unlikely some might seem; or to exaggerate to make a point.

Public attendance at these meetings would deter any augmentative techniques for fear of being misunderstood. To the contrary, in place of the rapid give and take among experts who need not articulate fundamentals among themselves, we would likely see drawn-out articulation of the most rudimentary matters merely to assure that the speaker would be fully

understood by his audience and by those who might read quotations from the discussion. We do not believe that the public interest would be served by substituting so much hot air for what is now effective governmental operation. On the other hand, fear of misinterpretation might lead to fewer meetings and more informal conversations.

Accordingly, I strongly urge that this bill not be enacted. If Congress believes that consideration of certain types of matters should in all respects be public, I suggest that legislation carefully limit these matters and spell them out with specificity.