



Statement of the U.S. Chamber of Commerce

ON: “Fixing the Watchdog: Legislative Proposals to Improve and Enhance the Securities and Exchange Commission”

TO: The House Committee on Financial Services

DATE: September 15, 2011

The Chamber’s mission is to advance human progress through an economic, political and social system based on individual freedom, incentive, initiative, opportunity and responsibility.

The U.S. Chamber of Commerce is the world's largest business federation, representing the interests of more than 3 million businesses of all sizes, sectors, and regions, as well as state and local chambers and industry associations.

More than 96 percent of the Chamber's members are small businesses with 100 or fewer employees, 70 percent of which have 10 or fewer employees. Yet, virtually all of the nation's largest companies are also active members. We are particularly cognizant of the problems of smaller businesses, as well as issues facing the business community at large.

Besides representing a cross-section of the American business community in terms of number of employees, the Chamber represents a wide management spectrum by type of business and location. Each major classification of American business -- manufacturing, retailing, services, construction, wholesaling, and finance -- is represented. Also, the Chamber has substantial membership in all 50 states.

The Chamber's international reach is substantial as well. It believes that global interdependence provides an opportunity, not a threat. In addition to the U.S. Chamber of Commerce's 115 American Chambers of Commerce abroad, an increasing number of members are engaged in the export and import of both goods and services and have ongoing investment activities. The Chamber favors strengthened international competitiveness and opposes artificial U.S. and foreign barriers to international business.

Positions on national issues are developed by a cross-section of Chamber members serving on committees, subcommittees, and task forces. More than 1,000 business people participate in this process.

Good morning, Chairman Bachus, Ranking Member Frank, and members of the Committee. It is an honor to be invited to testify at today's hearing: ***Fixing the Watchdog: Legislative Proposals to Improve and Enhance the Securities and Exchange Commission***. This is a subject that is of great importance to me personally. For 23 years I was an employee of the Securities and Exchange Commission ("Commission"). For 20 of those years I served as the Commission's Secretary. This was a position that afforded me a rare opportunity to participate first hand in virtually every aspect of the Commission's responsibilities. I considered it an honor and a privilege.

I retired from the Commission in January 2006. In the five years since my retirement I have been equally fortunate. I have had the opportunity to use the knowledge I gained at the Commission to advise government regulators in a wide array of countries. This experience has caused me to critically examine many fundamental principles of financial regulation, what it means and what it can accomplish. In addition to my international work, I have also had the opportunity to speak and write about financial regulation in the United States. In 2008, the U.S. Chamber of Commerce's Center for Capital Markets Competitiveness ("CCMC") invited me to conduct a study and write a report on how to improve the efficiency and effectiveness of the Commission. Released February 2009, that study, *Examining the Efficiency and Effectiveness of the U.S. Securities and Exchange Commission* ("the CCMC Report"), focused on the management of the Commission and three of its core responsibilities of the Commission:

- 1) the no-action letter process, primarily in the Division of Corporation Finance;
- 2) the process for reviewing self-regulatory organization rule filings in the Division of Trading and Markets; and
- 3) the process in the Division of Investment Management through which registered investment companies apply for and obtain exemptions from specific requirements under the Investment Company Act of 1940.

While I prepared the CCMC Report for the Chamber, I cannot take sole credit for its recommendations. The 23 recommendations, to improve the management and operations of the Commission, in the CCMC Report represent the collective ideas of more than fifty current and former Commission staff and Commissioners who agreed to be interviewed and who freely offered their ideas, insights, and criticisms. It is gratifying that, in the two years since the report was published, the Commission has implemented or begun to implement several of the recommendations. While some progress has been made, clearly transformative change at the Commission is needed

for the efficient and even handed regulation needed to have competitive financial markets in a global economy.

This statement and my testimony today also are based on an article I wrote in 2009, published in the University of Pittsburgh Law Review. The article focuses primarily on the Enforcement program at the Commission, a subject that I did not discuss in the CCMC Report. While the CCMC Report is based upon a series of interviews, the enforcement article is based solely on my personal views and research. I have previously provided the Committee's staff with electronic copies of both articles. Both documents are freely available on the Web sites of the U.S. Chamber of Commerce and the University of Pittsburgh Law Review.¹

I am currently conducting another study for the CCMC on the Commission. This study, which I hope to complete in the very near future, is examining the changes at the Commission since the last report. My goal is to provide a series of recommendations on the future direction of the Commission and what should be done to enable it to regain its status as an outstanding government agency. I hope that the upcoming report will be useful to the Committee in its ongoing efforts to oversee the SEC and to support vibrant U.S. capital markets.

Section 967 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("the Dodd-Frank Act") mandated that the Commission retain an independent management consultant to review the operations of the agency and recommend changes to improve its performance. Congress specified seven areas for the consultant to address. This Congressional directive was in direct response to a series of events during the past decade that raised legitimate questions as to the effectiveness of a government agency that for much of its history has been considered an exemplar of sound and effective government. In my opinion, it also exemplified what Congress should do when a government agency appears not to be performing effectively. Congress should ask important and tough questions and require sound and carefully considered answers.

Because of my continuing interest in the Commission, I shared the Congressional concerns embodied in §967. Having tried to examine many of the same issues myself I looked forward to seeing what an organization with the

¹ The U.S. Chamber of Commerce report is available at: <http://www.centerforcapitalmarkets.com/wp-content/uploads/2010/04/ExaminingtheSECRdcfinal.pdf>

The Law review article is available at:

http://lawreview.law.pitt.edu/issues/71/71.3/71_3_Katz_Reviwing_the_sec.pdf

reputation and resources of Boston Consulting Group (“BCG”) would learn and what it would recommend. Sadly, I was extremely disappointed with the result.

The BCG Report addresses the seven topics in a generalized and superficial manner that fails to inform, clarify, illuminate, or direct action. Its analysis and findings are largely conclusions, lacking in insight and devoid of empirical foundation. Its recommendations are so general they can’t be implemented.

Rather than attempting to summarize and critique the entire BCG report I am going to focus on its discussion of Commission reorganization, as this is the subject of today’s hearing. Following my comments on the BCG report, I will offer my perspective on the bills proposed by Chairman Bachus and Congressman Garrett. I will conclude with several recommendations to consider as Congress contemplates what actions to take to improve the performance of the Commission.

THE BCG DISCUSSION OF RECENT CHANGES AT THE COMMISSION.

The report identifies a number of positive changes in Commission operations designed to improve operations. These include the creation of Specialization teams in Enforcement, the National Exam Program in OCIE, the automated Tips, Complaints, and Referral System (TCR), and the creation of coordinating groups across divisions to reduce the silo problem.

Enforcement Changes

As the BCG report states, the Division of Enforcement appears to have made more significant changes than any other Division. The creation of units with specialized areas of expertise and responsibility is something that I advocated when I was at the Commission and something I recommended in my article on enforcement. Having said that, I do not know whether the change has been successful. Less than 20% of Enforcement staff is assigned to a specialized unit, and the number of cases these groups have brought is too small a sample to assess. So it’s difficult to determine what the impact has been. BCG, however, was not reluctant to reach a conclusion. “Some of these initiatives have been completed (e.g. the reorganization of Enforcement) and are already delivering good results” (p. 73). What measures did BCG use to conclude that they are delivering good results? Were the units compared in some way to the previous structure, or to the non-specialized units in the Division? It would have been useful if BCG provided some basis for the conclusion.

The Tips, Complaints, and Referrals system

In response to the perceived failure to act upon the tips concerning the Madoff fraud, one of Chairman Schapiro's first public changes was to hire a consultant to overhaul the system used by the Commission to record and process tips and complaints.² The highly publicized TCR IT project revamped the Commission's technology and cross-divisional processes for handling the approximately 300,000 tips and complaints it receives each year." While BCG describes TCR as "one notable success" (p. 44), there is nothing in the report that indicates that BCG took a close look at the system before concluding that it is a notable success. The report doesn't describe how the system is used or who uses it. We don't know how many people are assigned to analyze the 300,000 tips and complaints, where the function is located, and what types of analysis they perform. BCG does not provide any substantiation for its conclusion. Is it based upon a survey of staff using the system? Is it based upon examples of successful examinations or enforcement actions that were derived from TCR? Or is the conclusion based upon the fact that the project was completed? We just don't know. It reminds me of a similarly publicized IT project about ten years ago. With similar fanfare the Division of Enforcement hired a contractor to develop an automated system to surf the Internet and find securities frauds. That system was built and operated at a cost of millions, until it was terminated around 2005 when an internal review concluded that the system had produced almost no enforcement cases.

OCIE Risk-Based Examinations Program

The BCG Report states that "OCIE continues to refine its risk-based approach to the examination process. Examination candidates are now analyzed along a spectrum of risk criteria, which are cross-referenced with tips, complaints, and referrals to identify registrants with the highest risk profiles. From there, examinations are prioritized based on a further risk assessment of the registrants' business operations, among other factors" (page 173). This is another example of a broad conclusion that lacks supporting facts. Did BCG examine the risk-based model for efficacy? Are the risk criteria different from the risk criteria that OCIE has been using for nearly a decade? What results have OCIE achieved that demonstrates an improvement in the program? What are the further risk attributes that are used in the secondary analysis? The BCG Report doesn't ask or answer these questions.

Improving Coordination at the Commission

² SEC Revamping Process for Reviewing Whistleblower Complaints and Enforcement Tips, press release □2009-44, March 5, 2009, available at <http://www.sec.gov/news/press/2009/2009-44.htm>.

The Report highlights several changes at the Commission designed to promote a “culture of collaboration” (page 44). In addition to the development of the TCR system, BCG identifies other efforts to improve communication and coordination. For example the BCG report states

“The agency has also established cross-divisional task forces in other key areas of focus, such as the Consolidated Audit Trail and Life Settlements. In addition, a series of newly established meetings should help facilitate collaboration. Examples include:

- 1) the monthly “Trends Meeting”, which is tasked with promoting open dialogue about market trends, systemic issues, and key emerging/potential risks affecting the markets that the agency regulates;
- 2) the regular meetings of all rulemaking functions instituted by the General Counsel to align and ensure consistency of the rulemaking efforts resulting from Dodd-Frank provisions;
- 3) the regular meetings of the agency-wide “Task Force on International Implementation” established by the Office of International Affairs to discuss international issues arising from Dodd-Frank rulemaking and facilitate awareness and consistency, where appropriate, across the rulemaking process;
- 4) regular coordination meetings between OCIE and Enforcement to discuss the status of examinations and enforcement referrals; and
- 5) OCIE and policy divisions have implemented several new coordination mechanisms (e.g., “One Commission” supervision strategies for large firms).”

Having highlighted these coordination procedures, the report is devoid of any analysis of the impact of these efforts. Was a survey taken of participants to gauge effectiveness? Are there specific accomplishments that have come about because of these meetings? The report is silent. As someone who attended an uncountable number of coordinating meetings during my 20 years as Commission Secretary, my cynical view is that coordinating meetings are frequently excuses to avoid serious collaboration. In my opinion the silo problem at the Commission cannot be addressed by coordinating committees. Fundamental reorganization is required.

Because the BCG report does not provide any analysis of the impact of these changes, one must be wary of ascribing too much significance to these changes. Maybe they are successes, maybe they are not. BCG does a real disservice to the Commission and to the people who spearheaded these changes by failing to conduct a meaningful assessment.

Reorganization of the Commission

The Commission is long overdue for a careful reorganization. Its current structure is complicated, confusing, and inefficient. Even after the reconsolidation of the Executive Director and Chief Operating Officer offices into a single unit that oversees the five administrative support offices, there are still 17 divisions and offices that report directly to the Chairman, and an additional 11 regional offices that report to the Chairman for certain purposes and jointly to the Directors of Enforcement and OCIE for other purposes. Additionally there are the five new offices created by Dodd-Frank that will report to the Chairman when they are created and staffed. No CEO should be burdened with so many direct reports.

Moreover, the structure is antiquated. It is a structure built on a functional regulation model that was created to mirror the clear separations in the industries that it regulates. Unfortunately the Commission is organized for the capital markets of the 1970's. The clear separations in the financial services industry that existed almost 30 years ago are now a matter of history. The dual problems of a convoluted reporting structure and a functional regulation model that no longer comports with the regulated industries have directly contributed to the inability of the Commission to do its job well. Many of the people I have interviewed for the current CCMC study have described a personal horror story about trying to persuade Commission staff in separate divisions to work together and reach a decision. The fights between T&M and IM over the regulation of registered reps of broker-dealers and investment advisors are well known. So too are the problems between T&M and IM on regulation of exchange-traded funds. Similar problems arise between IM and Corp Fin on the regulation of hedge fund offerings. IM is interested in more public disclosure and Corp Fin is concerned that greater public disclosure may interfere with the private offering exemption under the Securities Act. Meanwhile, new products and new business models developed no longer fit into the old regulatory structures. Because the divisions compete to protect their turf, decisions aren't made and innovation is stifled.

How did BCG respond to the Congressional question on reorganization? It acknowledged the need for reorganization and identified three key organizational problems that must be addressed (p. 86).

1. *Structural design of operating divisions:* The Commission needs to address issues concerning the separation of broker-dealer and investment adviser regulation and the distance between exam and rulemaking functions
2. *Operations management and support office structure:* The Commission needs to ensure operational effectiveness and efficiency agency-wide as well as in the divisions and regional offices. In addition, the Commission should simplify its support office structure and empower the role of the COO.
3. *Strategy and design of the regional model:* The Commission should assess whether today's regional structure can effectively support the national programs it has created. In developing a regional strategy, the agency should focus on: 1) location approach; 2) the balance between, and roles of, regional versus home office staff; and 3) the regional reporting structure.

Having identified these critical problems, BCG described four options for reorganization (p. 89) to address the first problem³. However, the Report did not make a recommendation on which option should be implemented. Similarly it did not make specific recommendations on how best to solve the second and third problems.

Instead of proposing a solution to the three problems highlighted, the report took a bold leap and recommended merging the Offices of Legislative Affairs, Office of Public Affairs, and the Office of Investor Education! Not only is this an almost trivial recommendation, it is one that is based upon a superficial analysis that the offices should be merged because they all deal with the public. If BCG had done even minimal research they would have discovered that most government agencies separate the Legislative Affairs and Public Affairs functions. A bit more research into Commission history would have revealed that Legislative Affairs and Public Affairs were, at one time, a single office at the Commission. They were split into separate offices 30 years ago because the Commission concluded that interaction with Congress and interaction with the news media are actually very different functions, requiring different skill sets and different processes. Legislative Affairs is frequently a non-public, individualized, consultative process involving sensitive information that must be kept confidential. Conversely Public Affairs by definition concerns public information, and widespread and even-handed treatment of the media. The Investor Education office also has a very different function, with a different constituency. It is

³ One option, labeled 1c, mirrors the reorganization recommendation in the 2009 Chamber Report.

an intake process as much as it is a dissemination function. It must deal with a very high volume of inquiries and utilize standardized processes.

The failure to provide a careful analysis of the organizational problems at the Commission and make a comprehensive recommendation for reorganization is probably the most significant and glaring failure of the report.

However, while the BCG Report declines to recommend meaningful changes in Commission organization, it is not shy about making extravagant claims about the benefits of reorganization! According to BCG: “First, the initiative to implement a ***continuous improvement program***, such as lean process design, could potentially release up to approximately \$25 million in annual run-rate savings based on a very high-level estimate and BCG’s experience at other institutions. Second, ***the initiative to systematically redesign the organization*** could potentially release up to approximately \$25 million in annual run-rate savings, although there is potential for a lag between when the initiative is launched and when the savings are realized. Together, these two initiatives could generate up to approximately \$50 million in annual run-rate savings to the agency” (page 143).

What are the continuous improvement program and the initiative to systematically redesign the organization? Sadly, the report doesn’t provide a clear explanation. I suppose that the explanation of what it is and how it is to be accomplished will require another multi-million dollar contract. It is unclear how a consultant can decline to propose specific agency reorganization, but conclude that whatever reorganization is ultimately chosen and implemented could result in \$25 million in savings.

The SEC Modernization Act of 2011 (The Bacchus Bill)

As I have stated, the CCMC and I believe that careful and comprehensive reorganization of the Commission should be a priority. The CCMC report provides a series of specific recommendations on how to improve the management of the Commission, including specific ideas on reorganization, addressing inter-divisional stalemates, reducing the management burden on the Chairman, and creating staff, office, and agency accountability. Accordingly, the CCMC and I agree strongly with Chairman Bacchus on the need for real change at the SEC and look forward to working with him and the Committee to achieve this goal. I appreciate this opportunity to comment on the ideas for reform already proposed and to offer additional ideas for the Committee to consider.

As I stated in the CCMC report, the current organization of the Commission is designed to regulate the mid-1970's financial markets not the capital markets of today. This disconnect between the regulator and the markets and participants that are regulated has directly contributed to the Commission's regulatory problems.

However, while I support the objectives of the bill, I believe that the focus of the legislation should be reoriented to achieve the transformative change that is needed to restore the Commission as the world's preeminent financial regulator. Congress must be responsible for determining the authority and powers of a government agency, for monitoring agency performance and for holding the agency accountable for its actions. The government agency should be responsible for execution and implementation of its duties. This necessarily should encompass organization structure and assignment of duties. For the same reason, I believe that the Dodd-Frank provisions requiring the creation of 5 new independent offices is a mistake and should be corrected.

My second concern is a pragmatic one. Simply put, I believe that when Congress attempts to direct and control agency operations, the agency will always retain the capacity to comply facially but not in a meaningful way. An example of this problem is §965 of Dodd-Frank. This provision explicitly states that IM and T&M must have a staff of examiners that “perform compliance inspections and examinations of entities under the jurisdiction of that Division and report to the Director of that Division.” A person reading this provision would clearly assume that to comply with it the SEC would eliminate OCIE and reassign the staff into T&M and IM. Of course, that hasn't happened. As the BCG report explains, the SEC has determined to comply with §965 through a cosmetic change, rather than a meaningful change. “SEC management believes that the most effective and efficient means of implementing Section 965 would be to have a coordinating committee between OCIE, T&M, and IM and have a limited number of examiners in TM and IM whose function would include liaising with OCIE and supporting the coordinating mechanisms noted above”. (Page 45, footnote 86)

No organizational chart is ever perfect. It must change over time. If the structure of the SEC can only be changed by an act of Congress, we would be exacerbating the problem we already have. An agency that is slow to adapt to changing markets would become even slower to change. Going forward, it is important to recognize that the capital markets will always change and evolve at a faster pace than the regulatory and the legislative process. So any process that is adopted must be flexible and it must be nimble to allow the Commission to change and evolve with the marketplace.

Accordingly, I believe that Congress should outline a series of principles and objectives for the Commission to achieve, such as a defined chain of command, elimination of regulatory silos and improved coordination and communications amongst divisions, and a defined regulatory plan to promote market efficiency and capital formation. The Commission would be directed, within a specified period of time, to present a reorganization plan for Congressional review, consistent with Congressional oversight responsibilities and the long-established process for review of agency reprogramming requests. I believe that the broad outlines of this approach strike an appropriate balance between executive branch and legislative branch responsibilities.

Additionally, I believe that Congress could take several steps to improve the Commission. I offer the following five suggestions:

1. ***Amend the Sunshine Act to permit the full Commission (and quorums) to meet regularly with Commission staff to discuss agency operations.*** If the Commission could informally and confidentially meet with the staff to discuss agency operations it would greatly strengthen the role of the Commission. It would also provide a vehicle for resolving conflicts between divisions and offices. It is indeed paradoxical that the Chairman can call a meeting of key staff on a moment's notice, but only if other Commissioners are not present. The benefits of a collegial decision-making body are greatly reduced if the decision makers are excluded from taking part at early stages in analysis and discussion.
2. ***Amend the Exchange Act to require the Commission to include members with essential qualifications.*** Ideally the five-member Commission should include at least one member with accounting expertise, one member with relevant legal expertise, and one member with financial markets expertise. To improve agency management it may also be appropriate to designate one member as Vice-Chairman for management, as is done at the Federal Reserve Board, and require this appointee to have experience managing a large organization. The fourth Commissioner could be someone with credentials demonstrating expertise in investor protection.
3. ***Repeal the Dodd-Frank provisions stipulating the creation of new and independent offices.*** Congress should direct the Commission as to its authority and its duties and then hold the agency accountable for effective action. It is the responsibility of the executive branch to decide how best to accomplish its mission.

4. ***Create a Second Special Study of the Capital Markets.*** The final recommendation is, in my opinion, the most important. Fifty years ago, the Commission went through a similar period when it was viewed as ineffectual, understaffed, and outgunned. At the recommendation of then Chairman William Cary, Congress appropriated funding for a special team of experts to conduct a special study of the U.S. securities markets. At the end of its eighteen-month life, the Special Study team produced a five-volume report that formed the intellectual foundation for the Commission over the next twenty years. This is an appropriate occasion to undertake a second special study.⁴ Among the issues that should be addressed are the future of the U.S. and global secondary market structure, the interaction of the equity, debt and derivatives markets both in the U.S. and globally, and the development of a corporate disclosure system that reflects the needs of investors and the information technology of the present and future. An integral component of each of these issues is the regulatory agenda and operations of the Commission. The structure and role of the Self Regulatory Organization's should also be carefully examined.

H.R. 2308, The SEC Regulatory Accountability Act (Garrett Bill)

The Garrett Bill proposes to require the Commission to undertake a cost benefit analysis of all proposed rules prior to adoption. The Bill would also require the Commission to periodically review its regulations in order to determine whether they should be repealed or amended. These are important goals that I have supported personally and I know that the CCMC looks forward to working with Congressman Garrett and the Committee in achieving them.

The use of cost benefit analysis in rulemaking is a significant issue of public policy. It is particularly pertinent for the Commission in the wake of the recent decision of the D.C. Circuit Court of Appeals in *Business Roundtable and U.S. Chamber of Commerce vs. Securities and Exchange Commission* vacating the proxy access rule because the appellate court concluded that the Commission "failed once again adequately to assess the economic effects of a new rule".

Smart regulation requires a re-thinking of the process for developing and implementing regulations. A final regulation is the start of the process, not its

⁴ In 1988 when Congress enacted the Insider Trading and Securities Fraud Enforcement Act of 1988, it authorized the Commission to undertake a second Special Study. Unfortunately, funding for the study was never appropriated. For a detailed contemporaneous discussion of this provision see Kaswell, Stuart, *An Insider's View of the Insider Trading and Securities Fraud Enforcement Act of 1988*, 45 Bus. Aw. 145 (1989).

completion. While I have long supported the use of cost benefit analysis as one component of the rulemaking process, I have also believed that the process has limitations that are often overlooked. Cost-benefit analyses are and will always be fundamentally limited. They require estimates of the impact of events that have not yet happened. Simply put, it is difficult if not impossible for any regulator to know what will happen when a regulation is adopted. Capital markets are the reflection of large numbers of individuals making individual decisions. A regulator rarely has the capacity to predict with certainty how individuals or firms will respond to a new rule. If a regulator can't predict the response, it is difficult to accurately quantify the cost of compliance or quantify the value of benefits before one knows how the industry will achieve compliance. The current means of developing cost benefit analysis may be manipulated or fail to take into account facts that may not be readily apparent yet important to the ultimate purpose of a proposed rule.

For this reason, I believe in a different approach that combines a pre-adoption cost-benefit analysis with a post-adoption look-back requirement. In 2006, I described my proposal for a new system for developing regulations in a letter published in the *Wall Street Journal*.⁵

Instead of assuming, as lawyers do, that rules are self-effectuating, the Commission should adopt a scientific approach: Consider rules as working hypotheses. Whether the anticipated reaction occurs, and at what cost, is the empirical question. Under this approach, when the Commission votes to adopt a rule it would also vote to direct its staff to conduct a thorough quantitative examination of the rule's impact:

- 1) The Commission's Division of Risk, Strategy and Financial Innovation ("Risk Fin") would submit a plan to collect data on compliance with the rule, associated costs, and goals achievement. Merely developing such a plan will require the staff to articulate and the Commission to accept a statement of anticipated consequences.
- 2) It would also provide a plan for examining the data collected to enable the agency to examine the impact, costs and benefits of the rule. Making the Risk Fin division the focal point of this assessment would provide the agency's economists and industry specialists with substantially greater leverage in shaping rules in the first instance.

⁵ Jonathan G. Katz, Letter to the Editor, WALL ST. J., Aug. 8, 2006.

- 3) A timetable for the presentation of the results of these studies, in a published report that would be available for public notice and comment.

Under this approach, as an example, the Commission would collect data and re-evaluate a rule after a defined period, let's say two years, to determine the effectiveness of a rule, the need to keep it on the books, or to modify it. Such a periodic check of all rules would also help to determine if rules are obsolete.

This approach offers several advantages. In addition to compelling the staff to examine the rule's impact, it would fundamentally change how rules are developed. Knowing rules will be empirically examined will force the staff to carefully consider how this will be done and to develop internal discipline in the drafting process.

Institutionalizing a meaningful evaluative role for the Chief Economist will strengthen its hand during drafting of the rule. Finally, requiring the examination staff to consider these issues at the outset will cause it to be more pro-active in its inspection program, less inclined to focus on after the fact disasters and provide the Commission with more oversight of its function.

These recommendations will not result in more or less regulation, but instead they will achieve better regulation. Decisions should never be based upon a bias towards more or less regulation. Regulation must be based upon sound, fact-based understanding, and intellectual honesty. Most importantly, it must recognize that a free market is always changing in ways that can rarely be anticipated. There will rarely be a single correct answer. Regulators must accept that they will have a choice between reasonable alternatives. And when the markets move, the choice may change. So, regulation must be nimble, and regulators should never believe that they cannot or should not change as well.

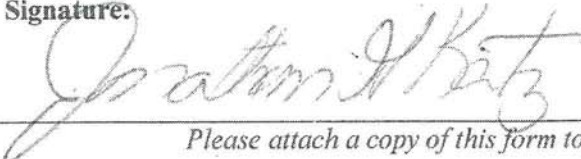
I believe that an amendment along these lines would improve H.R. 2308 and cause the Commission to incorporate cost benefit analysis as an integral component of an ongoing regulatory program.

Thank you again for the opportunity to testify and to give my thoughts as the Committee looks at means of reforming the SEC and its rulemaking processes. We need to have even handed efficient regulation that insures the safety and soundness of our markets. Having smart regulators using objective information is a key point in that process. There is a direct correlation between the world-class regulator and world class markets that we enjoyed for most of the second half of the twentieth century. Restoring our markets to that status will require transformative change at the Commission and I think that today's hearing is the first step along that road.

United States House of Representatives
Committee on Financial Services

"TRUTH IN TESTIMONY" DISCLOSURE FORM

Clause 2(g) of rule XI of the Rules of the House of Representatives and the Rules of the Committee on Financial Services require the disclosure of the following information. A copy of this form should be attached to your written testimony.

1. Name: Jonathan G. Katz	2. Organization or organizations you are representing: U.S. Chamber of Commerce
3. Business Address and telephone number: [REDACTED]	
4. Have <u>you</u> received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify? <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No	5. Have any of the <u>organizations you are representing</u> received any Federal grants or contracts (including any subgrants and subcontracts) since October 1, 2008 related to the subject on which you have been invited to testify? <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No
6. If you answered .yes. to either item 4 or 5, please list the source and amount of each grant or contract, and indicate whether the recipient of such grant was you or the organization(s) you are representing. You may list additional grants or contracts on additional sheets.	
7. Signature: 	

Please attach a copy of this form to your written testimony.