Speech by SEC Chairman: Remarks Before the Economic Club

by

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I'm delighted to be here this evening, because it's a great honor to address the Economic Club of New York. Over the years you've established yourselves as the foremost non-partisan forum for economic discussion in the country-and you've provided the venue for speeches by Presidents and Prime Ministers, not to mention the occasional SEC Chairman (I note there are at least three of us here tonight.)

This is a distinguished gathering — educated, accomplished, cultured. So you probably know that today is the birthday of that famous Norwegian artist, Edvard Munch. He's of course best known for his haunting depiction of existential anguish. You know, that familiar painting of cheek-slapping horror entitled "The Scream." Or, as I like to call it: "The Look of the Enron Investor." Alternatively, it could be called "The Look on Barbara's Face When She Sees the Bar Tab Tonight." In any event, happy Edvard Munch's birthday.

I'm very pleased to be here with national leaders such as you, Barbara; with my predecessors Bill Donaldson and Harvey Pitt; and with Bill McDonough, with whom I collaborated closely over the last several months of his tenure at the PCAOB.

This is undoubtedly the leading group of men and women in the financial capital of the most productive economy in the history of the world. And lest we take that fact for granted, it's worth dwelling upon for a moment. The American economy truly is a marvel. For some time now, our economy has surpassed most of the industrialized world — both in its rate of growth, and in its ability to create wealth.

Now, even though this is the Economic Club, I don't want to bury you in statistics on this point, lest I put you to sleep before dinner. But I do want to remind you of what you already know — that our economy's amazing capacity for growth holds vital meaning in very real ways for real people, individuals and families, whose lives and hopes and opportunities are directly tied to these numbers.

That's what it means that for many years now, economic growth in the U.S. has outpaced much of Europe and Japan. Our real economic growth has averaged 3.2% over the last decade, compared to only 1.8% for all industrialized economies. This year, it's averaging over 4% growth.

This audience, more than most, understands how that translates into the way people live — from improvements in our nation's infrastructure, to our security, to the education, health, and quality of life of every one of us. It's a measure of our ability to open our hearts. Our capacity to give. And our opportunity to research, and innovate.

America's businesses have created 1.8 million new jobs this year alone — and over 4.5 million new jobs since 2003. Payrolls have been growing for 30 straight months. Unemployment is lower than the averages of the 1970s, 80s and 90s. What else does our economy do that we take for granted? Well, we're the world's leader in farm exports. We produce enough food to feed our entire country, and the people of many other nations besides. We've been a net exporter of farm products every year since 1959 — an uninterrupted span of 44 years.

Our per capita gross national income, in terms of purchasing power, is fully a third higher than France, Germany, and the United Kingdom. That gives every American on average 33% more to spend and invest than the citizens of Paris, London, and Berlin, which may explain why the German government recently launched a $47 million advertising blitz — its largest public service campaign ever — to encourage Germany's citizens to cheer up.
Perhaps a 33% increase in purchasing power would work better. I know it would cheer me right up.

The fact is, per capita income in the U.S. is among highest in world. This exceptionally high income, in turn, improves America's quality of life. The United States spends about 5% of GDP — well over $500 billion annually — on environmental protection, more than any country on earth. That can't happen in nations without growing economies.

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As people head home for the holidays, there's a good chance they're headed to a home they, or their family, own. Nearly 70% of Americans now own their own homes — a far greater number, and a higher percentage of the total population than ever before. And of course, the highest in world. It is a privilege that we take for granted, but that is completely denied to the citizens of many other countries.

This sustained economic growth is all the more remarkable given our size — we have the third largest population in world. And because of the economic opportunity here, people are flocking to our shores. During the last decade, our nation's population increased 13%. That's five times faster than the percentage increase of all other industrialized countries in the world, combined.

So congratulations. You are all important leaders of this extraordinary economic marvel.

And yet you all know, that you're really not that much smarter, or more insightful, than the business leaders and investors of Britain, or Germany, or India or Japan. (Or at least that fellow sitting next to you isn't.) We've got to ask ourselves: what is it that accounts for America's superlative economic performance when compared to other nations? And almost any analysis of that question begins with recognition of the mainstays of America's free enterprise economy:

> The rule of law, the absence of corruption, bribery, and other forms of coercion by government and powerful economic actors.
>
> The climate of entrepreneurship that encourages men and women to take risks.
>
> And finally, a large, efficient capital market to finance it all.

The SEC has important responsibilities in each of these areas. Our law enforcement duties are an essential element of maintaining the rule of law in our nation's economy. Our powers to prosecute fraud and unfair dealing are guarantors against corruption and bribery. Our responsibility to exercise prudence and discretion in the use of those powers is key to maintaining a regulatory climate that is hospitable to entrepreneurship and risk taking. And our regulation of markets is aimed at upholding their integrity and efficiency. When distilled to its essence, the tripartite mission of the SEC, is to protect investors; to maintain fair, orderly, and efficient markets; and to facilitate capital formation — is really all about making America more productive.

Alan Greenspan, whose "two cents worth" are usually worth a lot more, recently said to me that the best investor protection is a growing economy and a rising market. Since we at the SEC most certainly are in the investor protection business, we've got to be vigilant in seeing to it that our actions do in fact contribute to America's productivity. To that end, all that the SEC does — or should be doing for our country — is meant to help create and sustain an environment that promotes economic growth.

So while we must all recognize the tragic fact of life that there is indeed fraud and unfair dealing in our capital markets, it's equally important to keep in mind, that there's a lot about our financial markets that is working well and that deserves the respect and support of our government. In other words, if it ain't broke, don't fix it. And when it does need fixing — and I know this from experience — the first rule of tinkering is to save all the parts.

That's especially important when it comes to regulating our capital markets, which perform such a critical function in our free enterprise system. Our capital markets serve to connect men and women in business enterprises large and small, with investors and lenders who measure the risks, accept the most promising, and reject the less worthy. This process amounts to a constant reallocation of capital — to the most promising and important uses, and away from the less efficient and less vital. It's a marvel that no central planning system could even hope to approximate. And the ultimate result is that our economy is more productive.

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That's why the SEC's mission statement requires us to facilitate capital formation. In our regulation of the nation's capital markets, the SEC is a partner in making America more productive.

I am absolutely convinced that our inspection and enforcement activities deter fraud; our regulation of the exchanges maintains orderly and efficient markets; and our disclosure regime helps investors make sound decisions. These are all essential aspects of well functioning cap markets.

But not everything we do is a net contributor to American productivity. Not all of the SEC's rules & policies are clearly written, and easily understood. Not all of the disclosure we mandate in our role as the "investor's advocate" is really useful to investors. I pledge to do everything in my power to correct that.

Since the day I began, I have been focused on translating legal gobbledygook into plain English. Clearly defined rules are necessary for people to conform their conduct to the standard the law expects of them. And clearly written disclosure is necessary for investors to gain the benefits of market information. When it comes to giving investors the protection they need, information is the single most powerful tool we have. It's what separates investing from roulette. If the SEC is truly to succeed in helping investors and in ensuring compliance with the law in the securities industry, we'll need nothing less than an all-out war on complexity.

It is, of course, true that a complex world often requires complex solutions. And certainly, there are desirable states of complexity-the ones that arise from a thing's intrinsic nature. DNA. A snowflake. Encryption algorithms. There, the complexity is essential to the function. But it's the contrived, artificial complexities that cause the problems, intricacy without function. Winston Churchill said it best: "However beautiful the strategy, you should, occasionally ... look at the results."

That, ladies and gentlemen, is what we're now doing at the SEC. We're looking at results. And what we're finding is that, in many cases, we're not getting the right results. The complexities of our rules too often add nothing to function. And that, of course, would be bad enough, even if the only thing it did was to annoy people and cut into our nation's productivity.

But more than that, we've found that complexity often impedes compliance even among those who want to comply. In other words, it's undermining the rule of law. What we surely want to avoid are rules so complex that they actually assist concealment of the very wrongdoing we seek to prevent. Complexity is great camouflage. I suspect that rules that run on confusingly, and at great length are the product of not just poor draftsmanship, but shoddy and hurried thinking. As Mark Twain once wrote in correspondence with a friend: "Sorry for the long letter. I didn't have time ... to write a short one."

Some years ago, under Chairman Arthur Levitt, the SEC began a crusade for plain English in investor documents. It was a noble first step that's been carried on by each of my predecessors here this evening. During my time at the Commission, I hope to advance this cause still further.

One of the ways we can do this is to reduce our use of jargon — insider shorthand that works in our own little circles, but effectively excludes those without the decoder ring. We can also express ourselves more clearly — with a view to providing clear standards for people to follow — rather than preserving future opportunities to play "gotcha."
To this end, at the recent AICPA convention, both FASB Chairman Bob Herz and I announced our combined efforts to combat complexity in accounting. This will be an across-the-board effort that will benefit issuers and investors alike.

We have other initiatives as well. When it comes to disclosure documents intended for investors, nothing is more complicated than the description of executive compensation. We aim to simplify it, and make it more meaningful.

Now, before you get that Edvard Munch look, let me be clear about what this does not mean. The Commission does not intend to, and never will while I am Chairman, dictate what any employee of a company makes — whether it's the CEO, or the mail clerk. Those are marketplace decisions. This is not about wage controls. It's about wage clarity. Information that's clear, complete, and comprehensible. That's it. We don't want to judge, comment, editorialize, pontificate, meddle, or otherwise interfere in salary decisions. And we most certainly don't want to cap salaries. This isn't the 70s.

What we will propose is disclosure that permits a complete and accurate understanding of the compensation package. Any judgment or action taken on that information is up to Boards of Directors and investors, not us. It is absurd to think that the owners of an enterprise should be denied full knowledge of how much they're paying their employees. The shareholders own the company, and the executives work for them. Think about it this way: Which of our nation's corporations issues signed, blank payroll checks for its employees to fill in the amount, learning only after the employee has cashed it, just how much that check was for?

Not only will improved disclosure of company information be useful to shareholders — it will also help directors by getting them better market information about executive compensation decisions in other companies. It'll help make their judgments better informed, and less susceptible to challenge in expensive lawsuits, that cost shareholders and companies alike.

It's been 13 years since the SEC last revised its rules for executive compensation. In that time, the nature of executive pay has changed drastically. The rules simply haven't kept up. The result is that too often, technical compliance with disclosure rules doesn't adequately capture the details of the latest compensation packages.

A proxy statement today may well contain all the required information, and yet still not tell anybody much of anything. Is it really disclosure if the investor has to sort it out and piece it together? Imagine the reaction from the press if I met their request for a transcript of every word in this speech. "There ya go. It's all in here somewhere." Technically, I'd have complied. In fact, I'd have provided nothing at all of value.

The message from that kind of disclosure is, at best, "You do the work." And at worst, it looks like "we're trying to cover something up here." Both messages are unacceptable. Investors and their directors have a right to the information. Complete. Clear. Comprehensible. It's quite simple, really. Investors should get all the information they need -and they should get it in a form they can use. If someone orders a steak, you don't give them a cow and a meat cleaver.

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Making our mandated disclosures actually useful to investors is the idea behind another SEC initiative -interactive data. The beauty of interactive data is that it will not only make today's 10Ks, and proxies, and mutual fund prospectuses more useful to investors — but it will also eliminate much of the time and expense that companies currently devote to filing SEC reports.

Today, the SEC has over 800 different forms. Each form is required to have its own cover page. The genesis of this requirement dates back to when reports were hand-filed in steel cabinets. Back then, the cover pages helped Commission staff do the filing — but today, they provide no useful information to the public, or to the SEC. Despite the fact that every individual company is required to file many different forms, these cover pages ask over and over again for the very same information in a slightly different format. In other words-more stuff no one needs, or wants. It's kind of like holiday fruitcake, in different colored cellophane.

If one goes beyond the cover pages to the entire form, to focus only on the truly unique info in each one, it's been estimated that instead of the 800 forms now required, the SEC might have need of no more than a dozen. The key to making this happen is looking at the data on the forms independently from the forms themselves. That's what we mean by interactive data. Computer codes can tag each separate piece of info on a report, and tell us what it is: operating income, interest expense, and so forth. That way, every number in a report or financial statement is individually ID'd: both qualitatively and quantitatively.

For individual investors, this means they'll be able to use more sophisticated software tools to analyze the information from SEC filings in real time. For the SEC, it means we could organize our database not by individual reports, but instead by companies who file them.

Obvious things — beginning with a registrant's address, its state of incorporation, and its classes of securities — wouldn't have to be repeated on every filing. The SEC would have that information already. This would eliminate duplication, and let registrants focus only on the updated information. We'd no longer need what we have today:

> 9 Securities Act registration statement forms,
> 3 Exchange Act registration statement forms,
> 2 annual report forms,
> 2 quarterly report forms,
> 1 current report form….
>
> … and a partridge in a pear tree.

Investors and analysts wouldn't have to hunt around for each separate form — all the information would be in one place, organized by companies. And I haven't even gotten to all the forms for proxy materials, annual reports, securities ownership, tender offers, and mergers and acquisitions. Today, every one of these forms has to be filed and processed separately. Rube Goldberg would be proud.

But the very best thing about interactive data is not just the form filing it will save, or even the time and cost savings for issuers and registrants. It's that the data will all be immediately accessible to investors, in real time. Today, the over 800 SEC forms result in some 700,000 reports being filed electronically on the SEC's EDGAR system. But EDGAR — for those of you who aren't securities regulation mavens, that stands for electronic data gathering, analysis and retrieval — is over 20 years old.

And a shortcoming of having such a fossilized system is that all of the info in these nominally "computerized" SEC reports isn't searchable. What's on file with EDGAR are just static reports — mere electronic reports of pieces of paper.

The result is that the investors and analysts who conducted 375 million on-line searches of the EDGAR database in fiscal 2005 had to manually re-type the information before they could even begin to use it in spreadsheets. (Or at least, they had to pay someone to do that for them.) The only way to make this less efficient would be to require the use of an inkwell and a quill pen.

Interactive data will change that, making the information in SEC reports immediately downloadable by investors and analysts the world over, via the Internet.

I'll mention just one more area where the SEC is moving to de-mystify disclosure for individual investors. Over 90 million Americans-representing 1/2 of all U.S. households-invest in mutual funds. Still more invest in 529 plans for college tuition, or in annuities for their retirement.

The SEC is moving to clarify the disclosure of the layers of costs and fees in those products, and of how those costs hit the investors bottom line. This improved disclosure will also clearly identify when a broker has a special financial stake in selling those products, such as the broker compensation system called "revenue sharing."

In proposing these improvements, we've been listening to investors themselves. We've assembled some exceptionally useful information through focus groups and individual testing.

They've told us that in order to be truly useful, investment information not only needs to be in plain English — it needs to be timely. So our new proposal will call for getting disclosure to retail investors when they need it most: at the point of sale. And it will permit using the Internet as the platform for providing point of sale disclosure. That way, mutual funds and other retail investments could make simple, plain English summaries available to individual investors, who could click through for more detailed information, if they wished.

More sophisticated investors as well as analysts and intermediaries, could find all the detail they wanted by drilling down into the densest minutiae. But because of the web-based disclosure, individual investors wouldn't have to be buried with information that they don't want and won't use. And all this can be done at considerable cost savings to both issuers and their investors.

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I'm very excited about these opportunities to make it easier and safer for Americans to invest. In waging this war on complexity, the SEC will be doing its part to increase America's productivity and the efficient functioning of our market economy.

Nothing that we do in our country impacts more people, or offers a greater opportunity to serve our fellow citizens than the improvement of our capital markets. They're the wellspring of support for our entire free enterprise system. And they touch the lives of almost everyone.

Whereas in Joe Kennedy's day, our first SEC Chairman could marvel that "one person in every 10" owned equities, today, our financial markets encompass the investments, the hopes, and the dreams of half of all households. 57 million Americans now own stocks — and median income for shareholders is a very middle class $65,000.

Our market economy, better than any other system in the world, enables the poor to rise from poverty, and enables the vulnerable and marginalized to be protected. Because after all, wealth must be produced before it can be shared.

To all of you, whose vocation it is to power this amazing engine of wealth creation with your imaginations and your willingness to take risks —

Thank you for what you do. Thank you for what you give each day for your fellow men and women, for your country, and for our world.

The SEC is honored to be your partner.

Check against delivery

http://www.sec.gov/news/speech/spch121205cc.htm
