

Securities and Exchange Commission Historical Society
Interview with Harvey Goldschmid
Conducted on June 17, 2013 by Robert Colby

RC: This is an interview with Harvey Goldschmid for the SEC Historical Society's virtual museum and archive of the history of financial regulation. I'm Robert Colby. Today is June 17th, and today's interview is being conducted in Mr. Goldschmid's office at the Columbia Law School in New York City. Mr. Goldschmid, thank you for being with us today.

HG: It is a pleasure to be with you.

RC: Where are you from originally?

HG: New York. Bronx, New York is where I grew up, in a working-class part of town.

RC: Growing up, did you have any interest in law?

HG: I did, although I'm not at all sure where it came from. There were no lawyers in my family. On the other hand, I was a history buff and read a lot of history and political science. Lawyers kept popping up everywhere in those works. By the time I was twelve, so far as my memory can reconstruct, I was pretty sure I wanted to be a lawyer.

RC: So you did your undergraduate work at Columbia.

HG: I've been at Columbia forever.

RC: (Laughter.) Were there courses or mentors that guided you?

HG: Yes. I was a history major. Richard Hofstadter was probably the most important influence on me, although ironically he almost dissuaded me from becoming a lawyer. I did a major writing project for him. The only class was to meet with him once a week or every other week. At some point along the way, he said that I really ought to do something more important with my life. I took him very seriously. For the first time since I was a kid, I began thinking about not going to law school.

RC: But you ultimately did go to law school.

HG: Ultimately, I did.

RC: What persuaded you not to pursue history?

HG: To this day, I love history in terms of reading, but there was more of an activist in me than in Richard Hofstadter. Now he could point out that he'd done many important things, in addition to writing great books. But for me, the excitement of being in the world more was I think what finally drew me. In part, I suspect, it was also the

psychology of having been set to be a lawyer since I was twelve; it was too late to turn back by the time I was a senior in college.

RC: Did you always plan to stay at Columbia?

HG: No. I went to law school here, went off on a clerkship, and then was an associate at a law firm. I thought at least initially that a firm life was where I was headed with an understanding that I'd spend at least part of my career in government.

RC: When you were doing your clerkship and with the firm, what were your primary tasks?

HG: The judge I clerked for was on the Second Circuit Court of Appeals and had been a Columbia professor. Judges in those days only took one clerk. Now they're up to four or five even in lower courts. So you did everything. You discussed cases after you'd heard the series of cases. He, of course, was the judge and I was the clerk, but we talked about how they ought to be decided. It varied, but very often I did at least the first draft of an opinion.

RC: What firm did you start with?

HG: I was an associate at Debevoise & Plimpton from 1966 through July of 1970.

RC: Did you focus on something particularly there?

HG: One thing that tempted me about going to the firm was that they had an open system so you could wander through the firm for two years. When I went there, I thought I wanted to do corporate and securities work, but I enjoyed my time in an early set of projects in litigation so much that somewhere in that first two years I became a litigator.

RC: Just doing all kinds of things?

HG: All kinds of things, although a major litigation that took years and ultimately went to Supreme Court involved the bankruptcy of the New Haven Railroad. As part of the deal to get permission for the Pennsylvania Railroad to merge with the New York Central Railroad and form Penn Central, they agreed to take the New Haven Railroad. They agreed on a price to be paid mostly in Penn Central stock. The New Haven presented – there were all kinds of issues – but a unique problem in how you value it. Various shareholders and creditors wanted more than the agreed upon price. The New Haven had been losing money for years. So the question was what value do you put on a railroad that consistently loses a lot of money? And then you think about, well, what are its assets worth? And then there were complexities with respect to the assets. The New Haven, in combination with the New York Central Railroad, for example, owned a large part of what is now, and was then I suppose, Park Avenue from the terminal up along Park into the Fifties. These properties earned a fair amount of money, but not enough to maintain the New York Central operation in Grand Central Terminal. So could you separate that

income stream, which was considerable, from its dedication, as we saw it, to paying for the terminal operation?

RC: So you would have been finishing this right before the bankruptcy.

HG: Yes, of Penn Central.

RC: So even as the negotiations are happening, the stock price is declining.

HG: Yes. I think the original value, don't hold me to it, was something like \$86 a share, as approved by the ICC. The value when we argued before the Supreme Court was probably about ten. It, of course, fell from there. We argued the case somewhere in the early spring of 1970.

RC: You said you developed an interest in litigation, but then you ended up coming back to Columbia. What caused you to do that?

HG: Well, it's a long story. While we were arguing this Penn Central case – at the Supreme Court we were given a good part of two days, which was very unusual – the justices probably didn't initially understand the case was realistically only about money. How much should be paid as opposed to how to keep the railroads alive? The railroads were going to run anyway. Somewhere during the course of the argument, Justice Black looked up and said, "You mean this is just about money?"

RC: (Laughter.)

HG: But anyway, it was an exhausting two or three weeks preparing in Washington away from New York. I came back and I had a whole thick pile of calls to return. One was from the chairman of the appointments committee here at Columbia. I expected he was calling about a friend who wanted to teach here, so I returned that one quickly. Instead, he asked whether I'd be interested in teaching. Columbia and other schools had been asking for a while before that. I said, "Gee, I've said no at least several times to you." He said, "Well, we wanted to try again." I was dead tired and thinking about Justice Black's question: "You mean this is just about money?" Anyway, I said, "I'd be willing to interview but remember, I'm likely to say no." So I did interview. The offer came. I thought I was going to say "no" for almost all of the two weeks I told Columbia I'd take before I decided. And somewhere in the last two days, things began to change. To this day, I couldn't tell you why. I could tell you why it's made for a great life but I couldn't tell you what changed my mind. But I did say "yes". This was 1970 and teaching was now ahead of me.

RC: What sort of things did you focus on teaching?

HG: This might have grown out of my interest in the turn-of-the-century issues in historical terms. Antitrust was a major area of interest. Columbia suggested that corporate law and securities would be a good place for me too. Those were the two main interests that I

came in with. Along the way in those early years, I also taught constitutional law and administrative law, but pretty well all through my academic life, antitrust, corporate law, and securities law have been the key parts of my teaching role and my scholarship.

RC: This is a time when the thinking on corporate law was changing. Could you talk a little bit about what the atmosphere was like in corporate law at that point?

HG: Well, that is the period where Penn Central went bankrupt. So in Corporations, the initial course which we still teach dealing with state corporate law and federal securities law, about 25 percent of the course dealt with federal securities law and 75 percent with state duty of care, duty of loyalty, merger and acquisition kind of things. Today, about 60 percent of Corporations, at least as I teach it, involves securities law. The major issues in corporate governance then, at least for me, were fears about the imperial CEO and what was wrong in terms of the checks and balances within the corporate system.

Penn Central, in 1970 when it went bankrupt, was our largest bankruptcy since the Great Depression; it was our largest railroad and our sixth largest industrial corporation. The questions were: Why did it fail? Where was the board? The governance of Penn Central was studied by just about everybody in the business school world and the SEC. The conclusion uniformly was that the board was perfectly ineffective. It was meeting roughly thirty or forty hours a year, couldn't possibly do the job in that time, and had no idea what was going on as the company slid into bankruptcy. All of that created a world

where we began asking about the imperial CEO, the role of the board, the role of shareholders, that kind of thing.

RC: I was going to say things like shareholder proposals are also an issue at this time. Is that something that you dealt with?

HG: Well, we began to, although they were just developing in many ways. It was during this period that Ralph Nader began his campaign at GM. That, too, added a set of issues.

RC: In '73, you put together a proposal on reforming corporate governance broadly. Could you tell me a little bit about that?

HG: That was one of the pieces I really liked because I had so little time to do it. It grew out of a speech I gave at a conference here at Columbia. I was just thinking through these issues and it forced me to sit down with pen and paper and state what was on my mind. I think we called it something like “the Greening of the Boardroom.” It was a set of ideas on where I thought things should go and what was wrong with the system.

RC: I know you put forward some ideas about the independence of directors and the role of how they were chosen. Was this an idea that the boardroom was the primary place where reform was needed?

HG: Yes, or at least a major place. If you think of the CEO and senior managers of the corporation in those days as relatively free from constraint – of course, if they did what happened with Penn Central, which went into bankruptcy, there were constraints – but short of bankruptcy, there was very little in the way of constraints on the CEO and senior managers. Duty of care cases seldom were brought, and absent special facts, almost never succeeded under state law. There was a piece done by a Yale law professor that said cases where anyone's held liable for failure to manage properly would be a very small set of needles in a very large haystack. That probably was overstating the number of needles.

The situation was one in which you first asked, in part growing out of the Penn Central failure, “Well, why can't we use directors more effectively? Why can't you get more out of them? How would you try to do that?” This was a principal focus of that piece and other work that I did. Other key issues that were raised were, “What about shareholders? Should they be the primary concern of the board? How important is long-term profit maximization?” issues we're still discussing. I'm doing a program at Columbia next week on the role of shareholders.

RC: There were other things in this time period after the Penn Central collapse that continue to drive this desire for corporate governance reform forward, I'm thinking mostly the corporate payment scandals and things like that. How did you view those? Did you expect there to be significant reform at that time?

HG: Well, you could feel people at conferences and roundtables thinking about the system and how it worked – at the extreme, Ralph Nader proposed to have federal incorporation, which really wasn't workable but indicated the concern. And we've had presidents for a long time raising issues about the need for reform of the state system going from Teddy Roosevelt to Woodrow Wilson.

The questionable payments were somewhat of a different set of issues. They raised serious problems, economic and social. It had become widespread, because there were five to six hundred major companies that reported under the SEC's voluntary system, for senior managers to think that everyone was paying bribes so we better do it too. Now in the real world, it wasn't at all clear that there was as much bribery as our executives thought there was. But since they suspected it, they felt they had to do it. And the more they did it, the more others did it. And so the Foreign Corrupt Practices Act, which came out of the SEC investigations and a so-called "voluntary" disclosure program, was a very healthy piece of legislation.

RC: The SEC followed it up with a long look at corporate governance and considered a lot of things, but ultimately didn't do a great deal.

HG: I think that's a fair evaluation. By the end of Harold Williams's term in the seventies, they had begun thinking about what ought to be done, about enhancements to disclosure, but relatively little had changed. In part, don't forget, this comes out of a philosophical position that said corporate governance is for states. Disclosure is for the federal system.

There wasn't much room in between. It was only as we got into the academic literature in some of the reform proposals that the push began. This was true of my colleague here, Bill Cary, who had been chairman of the SEC in the early sixties, but wrote in 1974 about enacting a federal minimum standards act. The twin themes of Bill's work and mine were to push towards reform of state law and, more importantly, to urge enactment of more federal law in the area.

RC: One of the things that's arising at this time is the market for corporate control, which has a variety of impacts on the way that management and shareholders interact. I was wondering if you could tell me, as this was ramping up, what was your perspective on that?

HG: Well, as often has occurred in my life, I looked at hostile takeovers with a kind of mixed view. The market for control really developed in the eighties, certainly most dramatically in the mid-eighties. In certain ways, it was a response to an industrial organization problem that developed in the sixties and seventies. In the sixties and seventies, the CEOs of almost every large corporation somehow got in their minds that they could manage anything, put together a drug company, and show business, and whatever else and they'd manage it well. A lot of those mergers, so-called conglomerate mergers in the sixties and seventies, turned out badly overall. A fair amount of economic review – Mike Scherer (Frederick M. Scherer) did the best work – indicated that even though some of the conglomerates were successful – and we think of GE today as a conglomerate and basically a success – by and large the whole movement was an economic failure.

Part of the hostile takeover bust-up scenario of the 1980s involved people saying, “You know, these configurations don’t work. We could do much better if we broke them up, and sold them off to people who knew how to run the various segments.” On that level, it was economically efficient and sensible. On another level, being able to replace that weak entrenched management and CEO was a good thing. But on still another level, some of the people who were involved in the hostile takeovers were perfectly unlovable. Some of it was created by easy money from Mike Milken's operation. I think of the hostile takeovers of the eighties as basically a mixed blessing. They sometimes went after inefficient, weakly managed companies. But too often they had the wrong people, tactics, and targets.

RC: As this is all happening, does it change what you're teaching at all?

HG: Oh, yes.

RC: How did I guess the way that you were thinking and then teaching about these issues change?

HG: When you're teaching at law school, fundamentally you have a title in terms of the course title, and then you figure out what you want to do with it. We call it Corporations at Columbia, which, as I indicated, is really state corporate law and federal securities law. There was a dramatic change to much more emphasis on takeovers, on proxies, on the

role of shareholders, on the role of the board, and movement, which is quite important on the whole, from a focus on state law to federal law.

RC: Because this is what the students are going to need to know or is this because what you're interested in?

HG: As I think about teaching, you're trying to do two basic things: first, give students the knowledge, skills, background to handle complex issues in areas; but the second more important part of university teaching for me is to think about not only what the law is, which students need to know, but what it ought to be. As areas opened up that presented significant legal, economic or social problems, those are the ones I wanted to spend time teaching about.

RC: It's probably helpful to think together and talk together about these things as well. One of the things that I wanted to ask about was during this time, you were a reporter for a the ALI Principles of Corporate Governance Project. Can you tell me about that experience?

HG: It grew out of being asked by a colleague at Columbia, Herb Wechsler, whether I'd be willing to be one of the reporters. I guess I was the first of the reporters and helped to develop the project. Basically, it grew out of the discussion we were just having about the need for some group to think through what we're doing with boards, what we're doing with shareholders, what we're doing with corporate goals, and what we're doing in the takeover areas. All were parts of that corporate governance project.

The ALI in many ways was a good group to work with. It had the cream of the Bench and the Bar and the academic community. It would be subject to pressure and was very much, in many ways, an establishment group but it also was thoughtful, honest, open to thinking through issues. The project created much more of a stir than I thought it would. In part, that resulted from the change of atmosphere in the 1980s.

RC: How so?

HG: The Business Roundtable is composed of the CEOs of the nation's largest say 160 companies. The original Business Roundtable, which I knew a little bit about, was formed in the seventies. Irv Shapiro, who was the CEO of DuPont, one of the founders, thought of it as a way of not necessarily saying "no" to every possible change proposal. The then-existing organizations in the business world were set up to basically say "no". The Roundtable, I think, was meant to be more flexible, more constructive, more nimble. Into the 1980s, the Roundtable had grown less willing to think about change. I remember someone who was senior in the group of CEOs saying at one point to me, "Now why are a group of law professors telling me how to run my corporation?" And members of the Roundtable felt that way very strongly. Of course, they weren't focused on the fact there were federal laws, there were state laws, there was a long history of the law being involved in corporate governance and the courts being involved in corporate governance. But it was kind of, "You can't play in our playground."

So it was very controversial on issues that, as you look back, you can't figure out why.

We made recommendations to have a majority of independent directors, to have an independent audit committee, to have duty of care standards which were relatively mild but had some contours, duty of loyalty standards, *et cetera*. Just about everything we proposed at the time is now in the law and taken as plain vanilla. At the time, however, CEOs on the Roundtable really considered it an "invasion of our territory."

RC: Those were the main targets that the ALI sought to address, the issues you just described about directors?

HG: Yes. The first substantive section was on corporate goals and purposes. The second set of segments were on corporate structure. That took into account the structure of the board and committees, that kind of thing. A lot of these were recommendations, not suggested as mandatory parts of the law. Part four, which I was in charge of directly, was on duty of care, business judgment, and the ability to delegate and rely. Part five was on duty of loyalty, which were basically situations in which there was a conflict of interest, directors taking something out for themselves or other kinds of conflicts. Part six, which only was partially developed, was on hostile takeovers. Part seven was on process issues and remedies of one type or another.

RC: Now were you involved all the way up until 1992?

HG: Yes, although I began to phase out my role. Part four was basically done by about 1985. I attended the meetings and did some of the planning but I was basically phasing out at that point.

RC: One of the things I've seen discussed is that in the midst of the ALI project is really when the law in economics movement took off and that caused some issues. Did you encounter that at all?

HG: I don't think of that as a great problem. I think of the opposition to what we were doing coming heavily from the business community. There was some overlay of law and economic critiques, but I don't believe that was a serious problem.

RC: Okay.

HG: Of course, some of the law and economic types, Dan Fischel and Frank Easterbrook for instance, would have argued strenuously for allowing hostile takeovers more room than I would have allowed, or the ALI would have allowed; certainly Fischel and Easterbrook wanted to make hostile takeovers far more potent than the business community wanted.

RC: One of the other things I saw that you were involved in in the eighties is the institutional investor project. Could you talk a little bit about how that came about and what that was meant to do?

HG: Yes. It was a particular interest of a colleague here, Lou Lowenstein, and Ira Millstein, who's a senior partner at Weil, Gotshal & Manges. Columbia Law School has a long history in the area, and in 2012, the Ira M. Millstein Center for Global Markets and Corporate Ownership was established to continue to deal with these issues. Ira, who is a close friend and teaching colleague, is one of the great figures in corporate governance and the law. As you began to think about the shareholder role and push for a larger role for shareholders, the fair question that came up in the eighties -- and again, now -- was, "Well, who are those shareholders?" There was already in the eighties meaningful movement from individual holders to institutions. So the institutional investor project was asking: who are these institutional shareholders? How important are they? What are the conflicts for the managers of the various intermediaries? What, if any, change in the law should there be?

RC: As you looked at this, what are some of the things that you discovered or noticed?

HG: The conflicts, of course, jump out at you. The people advising a pension fund, for instance, may be the same people who are advising a corporation and, while they claim to be independent, they are under enormous pressure from companies whose business they want. The same would be true of mutual funds and other major institutions that developed. There were questions about how do they vote, how do they decide how to vote, should we know more about their voting (which, actually, I had a hand in bringing about when I was at the SEC). There are all kinds of good questions and many still exist.

RC: We talked about corporate control. In the early nineties, there's a lot of discussion at the SEC about the role of shareholders.

HG: By 1991, '92, '93, boards were much more active and were asking questions. Then there was some change in focus to what role should the shareholders be playing. And in terms of both disclosure and encouraging institutional investors to be able to talk to each other, the SEC was doing good work in the early 1990s.

RC: Before I move on to some of the other things in the 1990s, I was going to ask if there were any other subjects from the seventies and eighties you would like to discuss.

HG: I think we've touched the big ones.

RC: Okay. One of the things that has struck me in looking at the 1990s is the issue of securities litigation. Can you tell me about your involvement in that?

HG: Basically, the issues raised about private actions were legitimate issues in many ways. I started out with the premise, which I still hold, that you need the mix of SEC and private actions to make the system work. To explain the philosophical underpinning on that, the SEC could bring in the 1990s maybe 400, 450 cases. Today, they've gotten up to 700-plus cases. The SEC has a limited budget, limited resources, and a limited ability to bring big and complex cases. To make the system effective in terms of accountability and deterrence, you need the supplementation of private actions. "Necessary supplement" is

the SEC's traditional language (and Supreme Court language) with respect to private litigation.

RC: Now generally, these actions are brought in response to fraud?

HG: Yes. It's financial fraud in IPO disclosure documents, periodic reports, or proxy statements. Insider trading has been a heavy area of litigation for the SEC in recent years and it usually acts alone in these cases.

RC: Was there something happening in the mid-nineties that made people think there was a need for reform in this area?

HG: The sense, and there was something in it, was that the private system was unaccountable. You have to take, again, a kind of historic view of the thing. When we talk about corrupt payments and the Foreign Corrupt Practices Act, the SEC had literally somewhere five, six hundred reports of these corrupt payments. Almost all of them were done "voluntarily" by private corporations. I think Stanley Sporkin, who was head of Enforcement at the SEC at the time, probably had a staff you could count on two hands. There was no way he could have done individual investigations in each instance. The creative use of respectable private law firm investigations and private actions was terribly important.

That remained true in the nineties in terms of this essential and necessary supplement, but many began to worry about how unconstrained and undisciplined the private system was. One of those truly embarrassing aspects of life for anyone looking at private litigation seriously was that the lead plaintiff's counsel in securities cases would be the law firm that was the first one to file at a courthouse. This meant, when wrongdoing allegations broke in the press, plaintiff's law firms would spit out boilerplate complaints and rush to courthouses; in the most embarrassing instances, with the wrong names in the pleadings. So the idea of a reform act in 1995 made sense. The lead plaintiff provisions in the PSLRA were a significant and helpful reform. Other provisions in the PSLRA, however, went too far in inhibiting private litigation.

RC: Now around the same time, you started consulting both for the FTC and the SEC. What led you to do that?

HG: I guess it's more or less personal. At the FTC, the chairman was Robert Pitofsky, who had been the dean at Georgetown. We were close friends and had been doing antitrust books together since 1975. And, as he had interesting issues, he would call and we would talk. And then we formalized it to a degree as he asked me to join various groups looking at high tech and other antitrust issues.

On a different kind of level, when Arthur Levitt was first nominated to chair the SEC, he called and said, "Can I come up and brainstorm with you." He was in the confirmation process. And we brainstormed some, and we kept talking after that with Arthur

periodically trying to get me to come to Washington. But I was on the other end of the phone with Arthur a meaningful part of the time in the 1990s and he finally got me to come down and spend time with him in 1997 or so. He persuaded me to come to the SEC as general counsel in 1998.

RC: One of the things I was curious about is that you and Ira Millstein worked on shareholder issues. Can you tell me a little bit about that project?

HG: Yes. Actually, that was not part of my formal consulting. And, Ira, I should explain, was the principal representative of the Business Roundtable in the debates about corporate governance and the ALI project. I think it fair to say that Ira now supports almost all of the key recommendations of the ALI Corporate Governance Project and his reform views go much further. Ira and I now teach a seminar in “the corporation in modern society” and have a wonderful time together in Columbia’s classrooms.

In that period, there was a real dustup about shareholder proposals and what they could accomplish; there was an attempt to cut them off in a way that I thought was unwise.

And at some point, Arthur called me and asked whether the two of us – I think he had the two of us in mind from the beginning – could work with a diverse group and see if we could bring compromise to the world. Both of us were touted as “nationally recognized corporate governance experts” and Ira, from his ALI opposition days, was considered close to the corporate community. So both of us took that on with an added proviso that we draft new 14a-8, the shareholder proposal rule, in plain English so that anyone could

read it, which was one of those good instincts that Arthur Levitt had. He's not a lawyer. His basic sense is that people ought to be able to read this stuff – – who are not lawyers – – and understand it. Even lawyers ought to read it without the unnecessary complexity and obscurity that often went into SEC drafting. So we did take it on. We had a group we worked with which had different perspectives; and we worked out what was a balanced compromise. But let me emphasize, I support Rule 14a-8 and what's behind it philosophically. I think what Ira and I did worked out very well.

RC: The issues were about?

HG: They fundamentally involved who could make a proposal and what bases for exclusion should be available. Logically, there certainly was a reasonable position in the corporate community that said, “Why should anyone with \$1,000 worth of shares, or \$2,000 today, be able to make a proposal and force everyone to vote on it?” And the answer basically was well, there aren't going to be that many. Overall there are 600 - 800 in any given year. Some of them get compromised and settled. For me, Rule 14a-8 had a wonderful therapeutic value. In the relatively insulated world of the board and CEO, you had a mechanism for raising serious issues and for making the board and senior management think more deeply about important issues. If no compromise occurred, you'd get a non-binding sense of shareholder sentiment.

Early on, so-called corporate responsibility proposals got few votes. There were 14a-8 provisions that said if proponents got very few votes, they couldn't make the same

proposal the next year. These were all precatory in general. Many of the governance proposals, again, helped to leaven the system. Should there be a poison pill, should there be a staggered board, should there be diversity on the board, issues of that type, it was healthy to be able to discuss them. Many of these types of corporate governance proposals soon were receiving majority votes.

RC: Looking at this from the outside, it also surprises me that there's a great deal of discussion about shareholder proposals and issues, but there's never that many of them. There are continuous claims of undue expense.

HG: There's little expense to it. I mean, what the shareholders are getting the right to do is put 500 words, in terms of a proposal and rationale, on the company's proxy statement. The company has to print the proxy statement anyway and mail it. So you're talking about printing an extra 500 words. Even if you get ten of them, it's not a very expensive process. Companies will say, "Well, but then we've got to answer and we've got to work hard." Well, they don't if they don't want to, but yes they'll almost always respond. Again, that's part of a process of thinking through that's healthy. But, in general, it's a relatively inexpensive process. It does take some focus away from the business, but it's a limited amount of interference. And again, the process is healthy, and there are permitted exclusions for small or inappropriate matters like those relating to "ordinary business." If it's relatively small stuff that the shareholders shouldn't be involved in, it can be excluded. There are all kinds of bases for exclusion.

RC: So shortly after this, you became the SEC general counsel. How did Arthur Levitt convince you to do that?

HG: I still wonder about that. Actually, it was a very interesting discussion in a way. He caught me somewhere, it must have been March of 1998, and asked if I'd come and be general counsel. I had been wandering to Washington, for part of a day a week, at the SEC. I had gotten some feel for the building itself at the time. He said, "You know, you can do this for a limited amount of time." We had two older kids who cared little if we were in New York or Washington, but we had one son who would be going into the seventh grade next year. I said, "Joe will absolutely hate this idea." Would you allow me to be general counsel for a year, only a year?" Arthur said, "Sure." If I had understood the job better, I'd have realized it's too complex a job to come in and try to accomplish all you want in a year. If he had been more candid with me, Arthur would have said, "Harvey, don't worry, once you're here for a year, I'll talk you into staying longer."

But I told Joe, our youngster, that he'd have an absolute veto on staying any longer than a year. We decided to do it. My wife Mary liked the idea, the adventure of moving to Washington. And so we came down for a year. As it worked out, I stayed about a year and a half and then became a special advisor to Arthur; I traveled to Washington two days a week for part of 2000.

But there was a wonderful crazy moment, which I'm not sure I should make public. Somewhere, it must have been February or March of 1999, where you had to make a

decision about school for the next year for children. Arthur came by my office and said, "I've got to talk to Joey." I said, "Sure, call him. What are you going to do with him?" He said, "I want to talk about why he ought to stay in Washington next year." I said, "Good luck, Arthur." He did call him. They worked out a meeting. It must have been one hell of a scene as this young kid, then a seventh grader, came bouncing into the Commission's building. The guards downstairs said, "What are you doing here?" Joe explained he was here to see the chairman. They looked at him. When they called upstairs, the chairman's staff came running down to escort this young, important man.

RC: That's funny. That's great.

HG: Anyway, Arthur and Joe talked for about an hour. Joe came out. My office was only down the hall. He said, "He took two calls while I was there. I know who Warren Buffett is but who is Phil Purcell?" At that time, Phil Purcell was head of Morgan Stanley.

RC: (Laughter.)

HG: I had warned Arthur that you don't change the direction of a kid in seventh grade who's gone to the same school in New York, with his friends, all his life. Joe wasn't willing to stay in Washington; he and his mother went back to New York and I stayed an extra half a year.

RC: Were there things in coming to the SEC you particularly hoped to address?

HG: I had a number of ideas. One ended up as Reg FD. Another area I knew needed work involved Rule 102(e), the basic rule by which the SEC could go after wrongdoing among accountants and prevent them from practicing before the Commission. Old 102(e) had twice been held invalid by the D.C. Circuit. Redrafting Rule 102(e) in a way that it would be both effective and fair -- and would be sustained by the D.C. Circuit -- was my first priority.

Corporate governance remained very much an interest. The functioning of audit committees and the accounting profession itself were major concerns of mine and Arthur's. So there were a number of things. I didn't come in with a sense of here's what I've got to accomplish, except for 102(e), which had to be revised. But I did have a sense of a lot of things where Arthur's concerns and mine overlapped.

I should add that, in general, working with Arthur Levitt was one of the great pleasures of my professional life. Arthur was an extraordinarily effective chairman. He has remarkable leadership skills, immense concern about investor protection and the integrity of our financial markets, admirable courage, and unmatched practical insight and wisdom.

RC: You talked about Reg FD as one of the things you had to deal with. Could you tell me a little bit about that experience?

HG: It was one of those fascinating issues that evolved from my teaching about insider trading and the securities laws. By 1998, it was clear that the framework for enforcing inside trading law was going to work. You could effectively go after what we called classical insider trading under the Supreme Court's *Dirks* case, decided in 1983. You could effectively now go after misappropriation, which was the other potential large gap, under a case decided in 1997, *O'Hagan*.

The big problem area in 1998-99 was what we all understood was going on, which was corporate executives briefing investment analysts about material developments as a way of currying favor or avoiding market volatility. The advice at the time from much of the Bar was that providing such material information selectively was okay under inside trading law. *Dirks* had suggested that giving a tip could make you vulnerable, but only if the tipper was doing it for "personal benefit" or "personal gain." In the scenario that went with FD, it wasn't for personal benefit. It was to enhance the corporation's place in the world, goodwill, relationship with analysts, *et cetera*. The Commission had a number of cases that were potentially available to try to expand *Dirks* to cover this corporate tipping, which had all of the drawbacks of insider trading. It made the markets unfair. It gave insiders an advantage. And to make it worse, if you were an analyst getting information from a corporate executive, it really did inhibit your ability to be critical. It was too important to be at the end of that corporate feeding chain. So there were enormously disadvantages to selective disclosure.

On the other hand, if we had been able to expand out inside trading precedents, it was going to create a very harsh world. We knew that a good part of the legal community, in terms of those advising major public corporations, was saying selective disclosure for corporate, as opposed to personal reasons, was okay. There'd be all kinds of lawsuits. Inside trading by then had been the subject, I think sensibly, of criminal action. One was afraid that if we won the test cases to go after this kind of tipping, we'd create a world with significant unfairness and traps for the unwary.

Instead, we decided that rulemaking was the best way to prospectively, fairly, and openly change the rules of the game. That was quite controversial at the time. Basically, Reg. FD said that if you're at the corporation and you have material information, you can't selectively disclose it. You've got to give it to the public at the same time as you disclose it to anyone from Wall Street. So the old idea of conference calls, which provided material information, for instance, limited to three or four analysts pretty well ended. Now conference calls are open to everybody. There's far more information out there. It's a much better and fairer world.

RC: You dealt with a number of other things. I think the aircraft carrier, you also were there during Gramm-Leach-Bliley. So you had quite a lot on your plate. (Laughter.)

HG: Yes. I kept saying, "Gee, it's busy around here." The aircraft carrier was well on its way before I got my hand on it. This was one of those things where Arthur Levitt said, "Get it finished for me." I would joke inside the building that the aircraft carrier was never

going to fly. It just had too much in it. We did get parts of it worked out for cross-border transactions and other things, but a comprehensive rulemaking would have been too much of a strain on the business community and everyone else.

Actually, one area that we haven't discussed, as important as any, involved working on accounting issues. Lynn Turner started as chief accountant at the SEC the same day I did as general counsel. Lynn, again, is a close friend and wonderful man, but he has a drive in him that's terrific in many ways but can scare people. Part of my job was to work with Lynn and make sure we were sensitive to other needs in government and not overly aggressive. This was a particularly sensitive time for the bank regulators who were worried about the banks in various ways. I spent more time with Lynn working with the Fed, the Comptroller of the Currency, the FDIC, and other regulators on accounting issues than I ever would have expected. I think overall it worked out very well. Often there were compromises that were in the public interest. Lynn, in general, was a great public servant.

Of course, Arthur Levitt had a large interest in auditing, accounting, and the auditing firms. He gave a terrific speech right at the beginning of my time, and Lynn's, on the accounting profession. This was, I guess, September in 1998.

RC: "The Numbers Game?"

HG: “The Numbers Game” at NYU dealt with accounting issues, the way the profession worked, conflicts within the profession, and improper techniques then in use. For banks, for example, “cookie jar reserves” was the terminology – – an improper technique – – that often came up. The SEC's view, which in the end was accepted by the bank regulators, was that you couldn't set up reserves in order to soften falls in earnings. Unlike what occurred in parts of Europe, our bank financial statements had to be transparent and clean.

RC: You started to talk about the auditor independence. Was that when you were the general counsel or the special advisor?

HG: Well, it carried over through both. The concern that all of us had, Arthur, Lynn and myself, was that the amount of income for audit firms coming from consulting was growing dramatically higher and was perverting the audit process. SEC enforcement decisions are made in closed meetings. It's one of the few things you do in closed as opposed to open meetings. One could see in those meetings, as one worked through a disclosure and financial fraud case, that the audit partners were under immense pressure and were feeling that pressure. The accounting firm itself might be saying, although not for the record ever, “We need to keep these people happy. We're earning twice as much for consulting as we do from the audit.” That just was a very unhealthy situation.

The question became, in part, how do you limit consulting, particularly the parts that had very little, if anything, to do with efficiency. It's one thing to say the auditor could do

certain tax work. There was an efficiency in that. But a lot of what was being done with computers and other things simply was making money for the auditor, in a way that was perverting the process.

RC: What were the major issues that you were working to overcome there?

HG: On the conflict situation, it was really refining what the auditor ought to be allowed to do for the audit client. It was okay if they did it for someone else. We worked out transaction guidance and rulemakings in that regard. There was a great deal of controversy. Significant limitations were incorporated into Sarbanes-Oxley, and in the end, added to by the Commission when I was serving as a Commissioner.

There were also issues about auditor and accounting profession regulation. Prior to Sarbanes-Oxley, there was a self-regulatory process that simply did not work.

RC: You're teaching at the same time as you're serving as the special senior advisor?

HG: Yes. Columbia was originally told I'd only be gone a year, and I was gone a year and a half. Arthur liked my company.

RC: (Laughter.)

HG: So I agreed to come back to the SEC twice a week during the first half of 2000. I was teaching full time and commuting down to Washington for two days a week.

RC: As you're back in the academic world, all the corporate accountability scandals hit in 2000, 2001. I would be curious to know what was it was like during those.

HG: Well, they really developed, in terms of public knowledge, as I remember, in late 2001. One had to be deeply concerned. I mean here I was having advocated throughout my professional life more active boards and more independent directors for oversight of CEOs and senior managers, which I thought was working to some degree. In the Enron context, governance reforms were not working. Enron had an independent board, on paper, and a good audit committee, which met the standards of the ALI. And yet we know what happened.

One saw problems with the other gatekeepers, with accountants, lawyers, and investment bankers. There was a sense that I had of systemic risk and systematic breakdowns. That's the way it looked. That's part of what tempted me to come back and serve on the Commission.

RC: That's what I was going to ask is you came back to the Commission sort of plop in the middle of all of this. What brought you back to the Commission?

HG: By way of background, the party out of power in the White House (through its Senate caucus) gets to designate, at least to some real degree, two commissioners. Candidates, of course, have to pass all the background and security checks and the rest.

Senator Paul Sarbanes, who I had gotten to know some when Arthur Levitt and I wandered the halls of Congress on Gramm-Leach-Bliley in 1998 and 1999, called me one day and asked whether I'd be interested in serving on the Commission. This must have been during the summer of 2001. I said "no." The response was because our youngster Joe was now a sophomore in high school, and I couldn't do it to him again.

Then by the fall of 2001, as Enron broke and one could see more coming, the need for thinking through these issues became more and more apparent. I didn't say "yes" immediately. What ended up happening was I was going to be in Washington anyway somewhere in those months. Senator Sarbanes and I met. We had a lovely talk. He's a terrific man. At the end of our talk, he said, "Okay, can I put your name on the list?" I said, "No." He asked, "Why not?" I said, "Because you're just making a list for Tom Daschle and the caucus. If I go home and tell my wife Mary I'm on a list, she's going to say "wonderful." She liked Washington. If I tell Joe, he's going to scream bloody murder, and I'm just going to be on a list. I said, "When you guys decide who you want" (they had two positions potentially open), "let me know and that's when I'll seriously consider returning to Washington."

RC: (Laughter.)

HG: Somewhere in January of 2002, I think it was, Tom Daschle called, this is making a long story shorter, and said that he was ready to recommend that the president nominate me. So we had a family powwow about it. I think because Joe was beaten up by his mother and two older brothers, he said he'd come to Washington. That's when I called and said, "Okay, you can submit my name." Then we went down to Washington to look for a place to live. Joe, who never backed away from his promise to come to Washington, was so sad.

It ended up with a family decision to leave what would be a junior in high school in New York. We were selling our house, which was near his school in the Bronx, in Riverdale. But his middle brother, Paul, and his older brother, Charlie, would both be going to Columbia Law School at that point. His middle brother would be a first-year student. We got an apartment for the two of them. I can't tell you how much money it has cost me to serve in government. But we got two of them an apartment at 116th Street, which had six rooms and good views of the river. Joe had a car because he had to commute back to Riverdale. They had an extra bedroom so my wife and I (she came up fairly often) could stop by at any time. But Joe remained in New York, and my wife and I came to Washington.

RC: Now I assume while you're going through the confirmation hearings and all that, you're keeping abreast of what's happening, especially with the Sarbanes-Oxley legislation progressing.

HG: Yes. And I advised on the legislation.

RC: When you finally get to the Commission, it's shortly after.

HG: Yes, I was sworn in the day after Sarbanes-Oxley was signed by the president.

RC: When you return to the Commission, what did you expect? I guess you kind of knew what you were getting into.

HG: Oh, yes. I mean it was perfectly clear, in addition to the scandals, that Sarbanes-Oxley was going to create a large amount of work. I knew there'd be much rulemaking and enforcement. And I did feel a basic responsibility to try to make certain that Sarbanes-Oxley worked.

RC: So with that in mind, what were the things that you really felt needed to be addressed first?

HG: Some of the deadlines were set for us. The centerpiece of Sarbanes-Oxley was the PCAOB, Public Company Accounting Oversight Board. We had to make the first appointments to that board, which had some real complications to it. That was certainly one major aspect of what we were doing.

RC: So you put the PCAOB together. How much of creating an organization, that was left to the SEC, essentially?

HG: It was an SEC appointment process. The SEC had basic powers over the PCAOB. The SEC had to approve its budget, *et cetera*, which was going to be taken largely from public corporations and the accounting firms. The PCAOB was going to organize itself, find its office space, etc. This was a new business starting from scratch.

RC: So you just had to sort of get it going.

HG: Yes, but finding the right combination of people for the board and the right chairman was complicated.

RC: Difficult. (Laughter.) So with the other sort of things you had to put together in terms of things like executive certification, disclosures, what were the most difficult, which did you see as the most needed?

HG: It's hard. The PCAOB, because it was replacing a self-regulatory system that was a basic failure, and because it was so important to inspire public confidence in the whole process, was a key. So clearly that had to be the priority. But you couldn't easily pick and choose. The kind of conflicts of the accounting firms (discussed earlier) had to be worked with in terms of establishing new rules based on Sarbanes-Oxley. Sarbanes-

Oxley was specific to some degree, but there were areas that needed elaboration or new detail. We had the power to do that.

In terms of disclosure, there were lots of things needed. Alan Beller, who was head of Corp Fin, was an excellent lawyer. Improving the 8-K and rulemakings on internal controls were major projects. The certifications, which became a technique used broadly, became a good way of getting compliances from the corporate community. I remember saying to someone on Capitol Hill, as Sarbanes-Oxley was being drafted, that the certifications from the CEO and CFO “wouldn’t really doesn’t change the law. But you can’t lose anything by putting in these certifications.” The CEO and CFO had been signing corporate disclosure documents for years. As the Ninth Circuit held in a case while I was general counsel, if you sign, you take legal responsibility. Words that expressly state, in effect, “we take responsibility” weren’t adding a heck of a lot.

But it actually worked out to be far more important than I would have thought. What happened was CEOs of major companies, and CFOs with them, began to recognize that when they were signing, they were taking legal responsibility for disclosure documents. That meant they began to say to those below on what basis are we saying this? What basis do we have for this number? And I think disclosure became meaningfully better. But it had much more to do with their understanding the function, the spotlight on it, than because of anything truly new in the law.

RC: One of the things you talked about earlier, and this goes back to the teaching aspect, is the shift of focus on state corporation law versus the federal securities laws. Sarbanes-Oxley is largely responsible for that shift.

HG: It certainly shifted a lot. Don't forget, much of this law comes out of Delaware. More than half our largest public companies are incorporated in Delaware. And other states follow Delaware's lead; there's very little corporate law spectrum in the United States. Delaware is a common law system. Basically, its judges decide cases. That means structural changes, for example, half your directors ought to be independent or your audit committee ought to be independent, usually will not come about under Delaware law. It's not how Delaware legislates or adjudicates.

So part of the way of changing corporate governance was to install some of these structural things by way of new federal legislation, SEC rulemaking, and SRO rules. Sarbanes-Oxley did create an independent audit committee. There were added provisions for independent compensation committees in Dodd-Frank. The lawyer ethical provisions came in Sarbanes-Oxley, where lawyers were required to "report up" corporate wrongdoing. Previously, lawyers had been regulated by state laws, which almost never worried about issues that involved large corporations. The basic state approach, in terms of the disciplinary process, was to prevent lawyers putting hands in the till, misappropriating trust funds, and matters of that type.

Section 307 of Sarbanes-Oxley (and the SEC's Section 205), along with SEC Rule 102(e), brought a meaningful part of the oversight of lawyers into the federal system.

The PCAOB, the centerpiece of Sarbanes-Oxley, went far towards federalizing the role of auditors. So, yes, there was a sharp movement towards federal law in areas that states had neglected.

RC: It's a long way from where you had been when you were creating your greening proposal thirty years before. (Laughter.) One of the other things that kind of parallels this is the reforms at the NYSE and the NASD. Talk a little about what seeing those was like.

HG: Well, again, the scandals at the turn of the 21st century – Enron, WorldCom and the rest – were so serious that everyone had to recognize basic failures. In governance terms, the New York Stock Exchange and NASD put in listing requirements for a majority of independent directors, an independent compensation committee, and an independent governance and nominating committee. Those were all good things to happen.

The use of the exchanges to change governance was a technique adopted by Arthur Levitt and the Blue Ribbon Committee he set up in 1998, where part of the reforms they recommended went into listing requirements. Officially, that Blue Ribbon Committee was established by the head of the New York Stock Exchange and the head of the NASD. The reality is that the SEC played a role too. The SEC had to approve the new rules. It was, again, another way of creating serious oversight.

RC: Now governance reforms are a big part of what you're doing but you also undertook a number of other measures on the Commission. I'm thinking of looking at the independence of research analysts.

HG: Yes. This is in 2002 and on. Another thing that you mentioned, I think I ought to go back to, is Gramm-Leach-Bliley. The truth is that Glass-Steagall, by 1999, had already been largely undermined by way of exemptions granted by the Fed and the Comptroller of the Currency. But whatever the merits of formally replacing Glass-Steagall, the SEC needed greater oversight of areas in the banking system that involved securities that we had been given no authority over. The rationale for not giving authority had been that banks weren't going to be able to sell securities. But it ended up they were dealing heavily in securities areas, but without significant oversight and without the SEC having authority.

So for the Fed and the Treasury an important part of what became Gramm-Leach-Bliley, revolved around who was going to control the banking system. Part of the reason it hadn't passed for many years, when I got to Washington, was because this fight continued. From our standpoint at the SEC, the trick was to be able to get oversight responsibility of things like mutual funds at banks, where we didn't have any authority. When Arthur asked me to take a major hand in this area, I said, "I don't know anything about it. I don't want to know. They've been doing this for nineteen years."

RC: (Laughter.)

HG: Arthur and I spent a great deal of time on Capitol Hill; it all worked out pretty well from the SEC's standpoint. From the nation's standpoint, with respect to Gramm-Leach-Bliley in general, one can argue.

RC: (Laughter.) Are you saying that that led to the issue of what are the other things that the SEC has jurisdiction over?

HG: Yes. The SEC got jurisdiction over a number of important areas, including bank mutual funds.

RC: Sorting out what that meant is one of the things that you dealt with as a commissioner.

HG: Yes, as a commissioner, we still had more to sort out in that area. Sarbanes-Oxley was a very thoughtful and, in general, well-drafted piece of legislation. As with all pieces of major, complex legislation, there's always a need to refine, to add, to elaborate, to pull back some at times.

One pull-back area, for instance, involved the audit committee. In the U.S. system, a worker or worker representative could not be part of an audit committee for his own company, nor could an inside officer. The rationale would be that there was too much prospect for them to be under the CEO's domination. They would not be independent. On the other hand, when you dealt with a German corporation, listed here, which had a

two-tier board and worker representation on the supervisory board, the issues were different. The question was should we be telling German corporations listed here that they couldn't have worker representatives on the audit committee? The answer was a prohibition just didn't make sense. The German system is different. The workers were more independent. So we carved out an exception to Sarbanes-Oxley for Germany. Invariably, any piece of complex, important legislation will need that kind of tinkering.

RC: I feel like Sarbanes-Oxley is one of the ones that keeps getting touched up or people are wanting to touch up.

HG: Yes, although it's Dodd-Frank that's the one now so much in the spotlight.

RC: That's true. You had mentioned earlier that one of the things that you looked at was the proxy voting records of mutual funds. Could you tell me a little bit about that?

HG: The question for their shareholders was how are they voting and what are they doing. It didn't make sense to me at least, and to the Commission in the end, for that to be done in the dark. We worked out a requirement for mutual funds to indicate how they were voting on shareholder proposals.

RC: Was there pushback against that?

HG: Sure.

RC: Their voting was already public. It just wasn't –

HG: No, it wasn't public.

RC: Okay. Interesting.

RC: Okay. Getting them to disclose it was, they thought that they could be pressured in different ways?

HG: For them, it was a hassle. It took time and expense if they were voting on 7 or 800 of these –

RC: That's true. You also, with regard to the mutual funds, looked at the governance and the independence of the directors for them. Could you tell me about that?

HG: As the scandals in mutual funds developed, you could see the boards not functioning very well at all. A mutual fund is an unusual institution because the investment adviser has such a dominant role in setting it up. And Arthur Levitt had begun to work on this: what were the functions of the board in the mutual fund context? As I looked at it, it became clear to me that the board had to have a check and balance function with respect to the investment adviser because, among other things, the board was negotiating the fees for

the shareholders of the fund. It was making sure things were running well and fairly. Independent direct oversight of the process was needed.

As we looked at the timing and late trading scandals, it was relatively clear that many mutual fund boards were not functioning well. We moved towards rulemaking in a number of areas; disclosure, use of compliance officers, and the independence of the chair of the mutual fund and of 70 percent of the board.

This was a recent issue with respect to JPMorgan and Jamie Dimon for instance. Should you separate out the chairman of the board from the CEO? In the public corporation context, one can reasonably argue both ways. One can argue that it's probably a good idea but shouldn't always happen.

In the mutual fund area, if the chairman of the board was the guy who set up the investment adviser and was now leading it, he had basic conflicts. His control over the board's agenda, and over information flows, was going to potentially be a problem. The case for a separation in mutual funds, as a bright line rule, really made sense to me, and to others, and the case for a largely independent board was the same.

Unfortunately, that the SEC's rules were rejected by the D.C. Circuit on a cost-benefit rationale. It's hard to know. We may have lost the battle but won the war in the sense that most mutual fund boards today are both independent, to the levels we wanted, and

have an independent chair. That rulemaking helped to bring the change about. But should it be a rule across the board? My answer today, as then, would be yes.

RC: One of the other things I was interested in is that the shareholder nomination of directors came up again while you were at the Commission and made some progress. I'd just be curious to hear what you thought.

HG: This goes back to my beliefs about accountability and governance. The hostile tender offer system was imperfect and a mixed bag. By 2000, it had largely disappeared anyway. Proxy fights have always been a largely non-viable way of changing management. The basic rules under state law are that the incumbents can spend relatively freely, or leave out the word "relatively," and do all the things of a normal political campaign from phone banks, to advertising; incumbents can hire all the lawyers and solicitors and everyone else they need. And the corporation pays for all of that while a proxy context is going on. For insurgents, they can spend as much as they like too, but they don't get a penny back unless they win and get a favorable shareholder vote. If they win, they'll get the shareholder vote. If you think of the cost of a major proxy fight, there are very few who can take the risk. For a large corporation, it's probably \$20-\$50 million at least, in a context where if the insurgents lose, they get nothing back.

The number of proxy contests has grown because of activist hedge funds in the last few years. For the most part from the 1990s through the early 2000s, there were few proxy fights. Most of those that occurred involved small companies. A few involved trying to

disarm a poison pill. But, basically, proxy contexts were not a viable way of challenging corporate managements.

The proxy access approach made all the sense in the world. For one thing, I like changing weak managements by way of the proxy system much better than by hostile tenders. In a hostile tender, it's money that's controlling the whole thing. In a proxy process, it's the current shareholders who can decide to change directions. They don't have to give up their shares. They don't have to give up their company. They just want to change direction. So it's always been a way to make a corporation's governance better.

I raised the issue inside the Commission. Our first proposal came out sometime in 2003. It was a very moderate draft. You had to own a substantial number of shares for a period of time to use the process, *et cetera*. It created a firestorm in the corporate community, particularly at the Business Roundtable, for reasons I have never completely understood.

So it was a complicated time at the Commission. There were relatively few ways of putting pressure on me. I often used to say: "I'm glad I kept my tenure at Columbia. I can say and do anything I think is right." For Bill Donaldson, who was a Republican, there was a White House and Treasury to deal with. There was a lot of pressure not to go forward in a context where the business community was violently opposed to proxy access.

RC: What is it about it that was troubling, do you think?

HG: I think, insofar as they understood what was involved, it was just the threat of taking the board, or part of the board, away from the CEO. By then, boards were far more independent. Directors were spending far more time. Today, we assume that in a large public corporation directors, on average, are spending 250 hours or so a year and doing their job in a serious way. But for the CEOs on the Business Roundtable, this was tampering with the critical source of their power. I don't think proxy access was going to lead to the firing of CEOs very often; something had to be badly wrong with the way a corporation was being governed and managed before those using proxy access could win. And then, under the SEC proposals, they would only get a minority of the board.

RC: Are there other things from your tenure at the SEC that you'd like to cover?

HG: We have discussed so much. The new disclosure enhancements were important. The role of the audit committee was very important in terms of rulemakings.

In Sarbanes-Oxley, Congress said very clearly that the audit committee must take direct responsibility – “direct responsibility” being the key words – for hiring, evaluating, compensating, and where appropriate, firing the outside auditor. That created a major change. As I look at the world today, while counseling an audit committee, for instance, dramatic changes have occurred. The outside auditor and auditing partner now think that their main responsibility is to the board and the audit committee, not to the CEO. That's

created a new dynamic in terms of the integrity of the process, the willingness of the auditors to be skeptical and question, and the candor of discussions.

RC: In 2005, you came back to Columbia. You had always planned on coming back?

HG: Yes, as I said, I kept my tenure. I've been here since 1970.

RC: That's remarkable. Did your experience at the SEC change the things that you taught?

HG: I've never quite figured out the mix of what I brought to Washington and what I brought back. But I certainly gained greater insight into how the regulatory world worked. Periodically as I'm teaching, whether Reg. FD, or the special insider trading rules (10b5-1 and 2), or other things that I had a hand in, I'll have to disclose my role to students under the Law School's conflict rules. This may add a bit to my credibility and student interest in an area; it certainly adds to my insight. On the other hand, much of what I did in Washington came from ideas that I developed while teaching. In my case, teaching and public service have worked together extremely well.

RC: I was going to ask what your perspective is on more recent developments in corporate governance in terms of Dodd-Frank and other things.

HG: I think Dodd-Frank's governance rules are quite good. On balance, I think Dodd-Frank made the world a better place. As you know, much of Dodd-Frank still hasn't been

implemented. We'll have to see how it works out. I was part of a group set up by the Council of Institutional Investors and the CFA Institute, the Investors' Working Group, that was co-chaired by Arthur Levitt and Bill Donaldson. We had proposals, in July 2009, that I think would have been even better overall.

RC: Not to ask you to speculate, but based on the direction that governance has gone in recent years, do you have thoughts on where it's going?

HG: I guess the largest governance issues out there revolve around the role of shareholders. In addition, a critical concern is how to get more focus on long-term profitability. For reasons I've never heard an economist explain to my satisfaction, there's a disconnect at times between short-term profit maximization and long-term profit maximization. In theory, at least, when shareholders or activist investors say to Apple or to some other company, "Take the money you have in the bank and declare a dividend," if that's a bad idea it ought to hurt the stock overall. In the long run, it's going to create an earnings flow that's not going to be what it otherwise would have been. But, for whatever reasons, there is disconnect; at times things that are not constructive in the longer term will push the shares up in the short term.

Part of what we need to think through now is how to discourage that from happening. What the nation needs is long-term profitability. But you don't want to excessively insulate management and the board by, for example, having elections only every five years. Thinking through how to get a greater focus on long-term profitability -- without

creating serious counterproductive effects -- is certainly one of the compelling governance issues of our time.

The other big issue that's out there (not a corporate governance issue) is how to adequately fund and organize agencies like the SEC. The current Commission budget is dramatically inadequate at about \$1.3 billion. The Commission is enormously behind any large Wall Street firm, let alone the aggregate, on its ability to invest in technology. We can't afford to have a global set of markets overseen or monitored by a Commission that's inadequate in terms of technology, resources, personnel, ,and overall budget. Dodd-Frank added greatly to the SEC's responsibilities. Congress has utterly failed to properly fund the SEC.

RC: Is there anything else you'd like to cover talking about?

HG: I think we've covered everything I know.

RC: Great. It's been a pleasure talking to you. Thanks for taking the time to talk to me.

[End of Interview]