

Securities and Exchange Commission Historical Society
Interview with Troy Paredes
Conducted on June 22, 2015 by William Thomas

WT: This is an interview with Troy Paredes for the SEC Historical Society's virtual museum and archive of the history of financial regulation. I'm William Thomas. The date is June 22, 2015, and we're in New York City. Thanks very much for agreeing to speak with us. We usually start with a little bit of biographical background, so maybe you could tell us where you're from and how you ended up in law, and securities law in particular.

TP: Sure. It's a pleasure to be here, and thanks for the opportunity to do this history. I'm from Southern California. I was born and raised in Southern California. I went to UC Berkeley and Yale for law school, and after law school I came back to California and practiced in a variety of different areas, but there was always a corporate securities dimension to my practice.

To be candid, there wasn't a particular event or spark that led me in the direction of corporate securities work. For whatever reason, early on I thought that I was going to be a lawyer and thought that I would be in the general area of business, and it turns out I stuck to that path and practiced as a corporate lawyer for a while before making the switch from practice to academia and then, ultimately, to government.

WT: So I see that when you were at Berkeley you did your degree in economics?

TP: Yes.

WT: And you got that in 1992?

TP: Yes.

WT: So you intended that as a springboard into business law?

TP: I intended it as a springboard into business law insofar as when I went to college I quickly had an expectation that I would be going to law school. But again, I can't point to any precipitating event that led to that decision. And yet, at the same time, taking economics was, for me, such a formative choice as compared to other majors. There's obviously a lot of terrific majors and disciplines, but the one thing that being an economics major challenged me with is a new way of thinking about things.

I've been asked from time to time from students who I teach and others, what's the most important class or influential class I ever took, and I think a lot of times folks may be thinking that I'm going to answer my basic corporate law class or my basic securities law class in law school. Although those were terrific courses, the class that always resonates to my mind as the most influential class was my very first class in economics, as a way of introducing me to a new discipline, a new way of thinking about things, which I think has carried through in terms of my private sector work, my government sector work, and it certainly had a big bearing on my work as an academic when I was at Wash U.

WT: I've noticed that in a lot of your speeches you refer to the economic consequences of regulation, and that does seem to be a theme that goes through a lot of your positions on various topics.

TP: As I think about that first economics class, it comes back to something that I did speak a lot about as a Commissioner, as well as law professor in my academic writing, which is the importance of cost-benefit analysis. There's a lot of ways to think about cost-benefit analysis, but in a very simple way it's thinking about whether or not the benefits are great enough to justify incurring the cost. And what you quickly realize—at least I did in economics—is that there's always cost and there's always a benefit, and the ultimate question is how are you going to trade those two things off against one another? And you add to it a notion of a marginal analysis with a marginal benefit and a marginal cost of doing one more thing. For me, it was a really eye-opening way of thinking about things, because it's to say that just because one unit of something is good it doesn't mean that two units of that same thing are worth doing, given the cost that you may have to incur as a trade-off. That really was, again, a new way for me to think about things and inform my thinking on everything I've done since.

WT: So then you decided to go to Yale for law school, across the country. What brought you to Yale specifically?

TP: It's a terrific school, and that was the big draw. It was just the chance to be at an institution like that with the faculty and with the other classmates I would have. There of course are a number of terrific law schools around the country, but it was the chance to be there for those three years. One of the things that I really enjoyed about the experience is the way Yale is set up it affords you a lot of flexibility to focus on the things that you find most interesting. I found myself—and this was not a reason I went there but it was something that I was welcome to find out once I got there—was the chance to do a lot of writing, the chance to do a lot of research for different papers and classes, which I think is what ultimately lit the spark to make the shift to being an academic.

WT: Let's talk a little bit about your law practice first. Could you give me a general sense of what that entailed?

TP: Sure. It was a pretty far-ranging practice, insofar as there were a number of different key pieces to it. One key piece was, at that time California was going through a restructuring of the electric industry, in the mid-'90s and late '90s, right when I was graduating from law school. I happened to have had an interest in regulated industries, in the electric industry, the energy space, and so I ended up going to a firm that did a lot of work in that particular space. It meant that a sizable part of my practice, at the time, was focused on transactional and some regulatory commissions of the restructuring of the electric industry in California. So that was very interesting. In addition to that, there was a lot of finance work, particularly representing banks on the LBO side of things. I did a lot of work representing banks and financings.

I also then had a general corporate practice, so it could be asset transactions, purchase/sale agreements, shareholders agreements, corporate governance, corporate formation, so a wide range of things. I felt privileged to have the chance to get exposed to whole different areas of transactional and corporate practice with some regulatory overlay. It was hard to get bored when there was so much going on, and, again, a wide array of things that forced you to constantly be learning new things and thinking about new challenge and opportunities for your clients.

WT: Did you get involved in anything like the Bar Association that would eventually lead you into the more academic direction?

TP: I didn't.

WT: What was the law firm's name, by the way?

TP: It was a few different law firms. I started at O'Melveny & Myers, and then I ended up going to Steptoe & Johnson for a bit, and then I wound up my career practicing at Irell & Manella, and then it was from Irell that I ended up going to Wash U.

WT: So tell me how that came about, then, going to Wash U.

TP: I'd been practicing for about five years. I was a fifth-year associate, and thinking back to what I was doing when I was in law school, which was a lot of research and a lot of writing, I realized that I was reaching the point that if I was going to be an academic, or try to be an academic, that I needed to make that decision sooner rather than later. So, as I thought about it, while I was enjoying practice, there was something about at least having the occasion, the opportunity to think about things in a different way, to think about things in a way that an academic is asked to think about things, if you will, the questions of what should the law be, thinking about policy and philosophy and theory as well as practical applications.

Since I was looking for the occasion, was interested in tackling those sorts of questions, and given where I was in terms of the number of years I'd been out of law school, I decided it was time to make the jump to academia. So I put my hat in the ring, and ultimately ended up landing in Wash U in Saint Louis.

WT: So, you were exclusively focused on securities law then, as a professor, or was it broader?

TP: It was broader. My work as an academic, my scholarly work, my writing, was in large part securities regulation, as well as corporate law, corporate governance, but also property theory, administrative law, administrative agencies. At the end I was doing more in the intellectual property space as well. A lot of my work was grounded in behavioralism, or behavioral law economics, or law psychology, or behavioral finance—

it has lots of different names that it goes by. My writing was across a number of different areas, which again I think for me was interesting because it gave me the chance to think about a lot of different questions and draw on lots of different literature and learn from lots of different disciplines, and to try to bring that all to bear in the context of whatever the specific issue was that I was taking up as an academic, in terms of my scholarly work.

When it came to my teaching, my teaching was more focused. Ultimately, when I arrived at Wash U, I did teach the first-year property class for a handful of years, but my core teaching responsibilities were the basic corporate law class, the basic securities law class, as well as a seminar on those sorts of topics.

WT: So, tell me a little bit more about behavioral economics, or whatever we want to call it, and some of the research that you did in that area, how those concepts formed the basis of your research. That's very interesting to me.

TP: Sure. There's really two strands, but I'll start with the more basic observation as to why I started to think about behavioralism, law and psychology—again whatever one wants to call it. When I took a step back and started thinking about what to write on, one of the points that became clear—at least the way I express it these days, I'm not sure I expressed it the same way at that time—is the very simple question of why do we even have rules, regulations, and law? What's the point? What's the purpose? And the point, the purpose is, I think, to change the way people behave. The essence of deterrence, frankly, is about behavioral change.

We could think about it, though, beyond simply the terms of deterrence. So, for me, what that then meant is I needed to have a richer understanding of the ways in which individuals and groups of individuals actually behaved, which is to say actually made decisions. So, as I started to focus on that beyond one's own intuition and one's own experience and anecdotes, you realize there's a very rich, and today even richer, literature in psychology and economics that focuses on those sorts of questions. In fact, more recently, Nobel Prizes have been given out to folks whose life has been dedicated to those sorts of insights and learning and understanding.

So, for me, how that particularly played itself out is in the context of two strands of research, which I'll just mention briefly. One is, I have now for several years been thinking about the so-called problem of information overload in the context of securities regulation, and that stems from an extensive literature looking at the ways in which individuals in different settings make decisions in the face of more and more information, and how the decision-making strategies that individuals bring to bear changes as a function of the amount of information they have to process.

This has its roots in the seminal work of Herbert Simon, who himself won a Nobel Prize in economics, if I recall correctly. I got turned onto that literature and started asking the basic question of, well, what does that mean for a regulatory regime, which, at its core, is about providing investors, in the case of federal securities laws, with more and more information? Does it challenge the basic premise of the federal securities laws that more

information is always better than less, once you think about the ways in which individual investors, let alone groups of investors, actually make decisions?

So that was one way in which behavioralism, psychology, judgment was something I drew on in terms of my work in the context of securities regulation. I wrote a paper and I continued to write in that area and think about those topics.

WT: Before you move on, can I ask if, in addition to engaging the law side of the equation, you engaged the economic side of the equation, where a lot of the models right now are based on things like rational actor theories and the optimized use of information?

TP: You're exactly right. The literature that I drew on for the work I've done is sometimes coming out of psychology departments and sometimes coming out of economics departments. It is something that speaks to, as you said, the assumption is about the rational actor model as compared to the ways in which literature and more recent learning suggest that perhaps we don't always act the way that that model predicts. Then the question is, how does that inform our assessment of what the law ought to be? Because, as you have a richer or different understanding or set of expectations around how individuals make decisions, that then strikes me as flowing back to give us at least some reason to reassess the legal regime, to make sure that you actually achieve the outcomes you want, and you don't miss the mark by misunderstanding what the likely behavioral response would be in response to some regulatory change.

I would just be quick to note by way of caveat, that one, at least in my view, has to be very careful about the kinds of conclusions one jumps to and the degree of extrapolation. Any time you're using literature like this, or literature which is based on what happens in an experimental setting, for example, there are a lot of caveats because those findings don't always translate to the real world or translate to other contexts. But, nonetheless, it provides something to think about as you think about what the rules of the road ought to be.

In the context of corporate governance, I focused on CEO decision making and the dynamics within boards, as well as the dynamics between boards and CEOs. This is another hot area for the last number of years, thinking about some of the ways in which upper management and organizations make decisions, the ways in which groups of individuals—call them boards of directors—would otherwise interact and engage, and what the implications then are when it comes to governance structure, governance practices, modes of engagement among board members, and between directors and board members and the CEO. Again, it's another area that's received a lot of attention in recent years.

So this interest in behavioralism, let's call it, is something that's played out both in terms of my scholarly work and securities regulation, but also in terms of corporate governance.

WT: It's a subject that I would love to talk all day about, but I guess we better move on. One of the things, of course, that you've done is to take over the fourth edition of *Securities Regulation*, Loss and Seligman. Could you tell me how that opportunity came to pass?

TP: I did come on the treatise with the fourth edition, and I then had to take a hiatus when I was serving as a Commissioner, but I'm now back on the treatise and actively engaged as one of the coauthors with Joel Seligman. The way it came about is pretty straightforward in the sense that Joel, who had been brought on by Louis Loss beforehand, was my dean at Wash U. I think it was my fourth year or so there at Wash U, things lined up and Joel asked me if I'd be interested in coming on as a new coauthor, and I said yes, and that was it. I joined, had a few years, I think, under my belt on the treatise, and then the occasion to go to the Commission presented itself. So, as I said, I took a hiatus from the treatise, but I'm now back at it.

WT: What year was it?

TP: I joined the treatise in 2005, went to the Commission in '08, and am now back at it.

WT: You started at Wash U in 2001?

TP: I started at Wash U in 2001.

WT: What were some of the things that are going into the new edition? Obviously you have things like Sarbanes-Oxley, various new rules and so forth. I expect that your particular philosophy of law is not quite the same as Seligman's. Did that work itself into the dynamic at all?

TP: You're an astute observer. I have terrific regard for Joel, but I think it's fair to say that we may sometimes view some of these questions differently. But that has never been a problem, and I think what that, at least from my perspective, reflects is the effort of the treatise to try to call it as straight as one possibly can and to be balanced in the presentation, and to try to collect and capture what's going on in securities law and reflect that to the best of our respective abilities.

And so personal policy preferences, or views, or philosophy of federal securities law or whatever it may be, to the extent we may come out differently on some of those questions, never whatsoever presented a difficulty or friction as we've worked on the treatise again.

WT: Were there any particularly interesting areas that you were working on revising for the fourth edition that stand out to you in any way?

TP: Well, everything (laughter) is interesting in its own way, when you think about it. Part of it is because the entirety is really a system that, from my perspective, needs to work as a whole. So, when you think about the complete system that is the federal securities laws,

it makes each piece interesting unto itself, but interesting as you try to put together how it fits into the broader regulatory landscape.

One of the things about the treatise, both when I was at Wash U and since, is just the sheer rapid pace of change and the volume of change over the last handful of years—even before that, but if you think about the amount over just the last few years! I'll just give one quick example. If you think about the capital raising process, for example, under the '33 Act, well, that changed meaningfully with the JOBS Act of just a few years ago. Think about if you try to update the treatise to try to reflect all of those developments, that's a lot of work, but that's a high-profile change.

But I recall some very substantial rulemakings that I was trying to integrate into the treatise, which were important in the context of securities law but weren't getting the kind of widespread attention as some recent developments. But when it comes to actually doing the work on the treatise, those are challenging and consequential, too.

So, it's a fascinating occasion to have the task, if you will, of keeping an eye on what's happening across the landscape of securities regulation. And again, for me, because I do think of securities law as this kind of system, that it's my inclination to want to think about it that way. The treatise certainly forces that as you're trying to keep on top of everything that's going on as best as you can.

WT: Can you offer an example of one of those less prominent issues that nevertheless had to be grappled with?

TP: I'm trying to think back to when I was updating the treatise, which was about ten years ago. Well, there had been some changes, when it came to the public offering process, that were very much written out of the SEC. So, when you think about a rule, when you think about any rule, and increasingly they become lengthy, think about a rule release that's five, six, seven hundred pages, and all of that is rule text. A lot of that is explaining the rule, talking about the comments and the like that helps you understand the choices that were made, the exercise of sitting down with a 500-page release, trying to integrate it into a text, that's a challenge.

WT: One of the things I wanted to ask you about, in terms of your general philosophy of the law of securities, is your opinion of principles-based regulation. Some people who are concerned about too much granularity in the regulation or overregulation fall back on that. I didn't get the impression from your speeches that that was necessarily a solution for you, but I'm wondering if you could offer your opinions.

TP: I do worry about overregulation. Almost in every speech I gave, particularly post-Dodd-Frank, I probably talked about my concern in one way or another about overregulation. But, when it comes to the question of being more principles-based versus rules-based—this too we could have a very long conversation about, but a couple of quick observations. One is, oftentimes rules that start out as more principles-based start to take

on a more rules-like quality, whether that's through guidance, or whether that's through understanding, or whether that's through nudges. I think you have to think about, at least from my perspective, principles-based and rules-based not only as itself a continuum, but also things that may start out as principles-based, how is it likely to play out over time, and will a principles-based approach persist or will there be a tendency for it to start to take on a more rules-like quality?

Then secondly, the virtue, I think, of a principles-based approach is that it allows those subject to the regulations some flexibility to come up with compliance approaches that make the most sense for their enterprise, that work best for their business, that work best for their governance, that work best for their customers, and for investors and their position in the marketplace. One-size-fits-all prescriptive approaches just about never fit all, and in many instances may not even fit many. But a challenge with a principles-based approach is that it provides room for you to be second-guessed after the fact on the choices you made. You have not only the risk of being second-guessed, but, number two, you have the uncertainty as to what's going to satisfy the regulators when you're trying to put in place a compliance regime and approach that you think is right. But, because you rarely, if ever, can achieve zero risk of something going badly, you have the risk of being second-guessed with the benefit of hindsight by regulators or others, and you have the uncertainty.

I think there's a lot to recommend a principles-based approach, but I think one has to have in mind the ways in which that principles-based approach is enforced. Is it

enforced, if you will, through a more prudential mechanism, that is to say so long as a company has demonstrated good faith effort to really try to get it right? If there were some mistakes along the way, even what some may say is a violation along the way, is that going to be worked out through a chance for them to rectify it and figure out what changes need to be made going forward? Or is it going to be addressed through an enforcement action? I think that has to be part of the equation in terms of how you think about what the regulatory response is to a principles-based approach if things don't quite go the way one would hope.

WT: Focusing in on one of the things that you said there, I gather that you would put a particular stress on self-regulatory organizations, professional and industry groups in order to set best practices.

TP: I think industry groups or SROs that have a keen understanding of the business and what's reasonable and the trade-offs can be extremely productive. But I think whether one's talking about a self-regulatory organization, or one's talking about some other kind of industry group, or one's talking about the government, one can have general thoughts. The details, of course, matter a lot, and without knowing exactly how something's going to play out in fact and on the ground, I think it can be difficult to come out in favor of one thing or another.

I think rather these are all options, these are all levers, these are all modes of trying to craft the proper regulatory regime, and then it's a matter of thinking through the details as

to what's going to work, what's going to work best. But, for me, I have as a background concern, when it comes to all of this, worry that, certainly now but even in other periods, that the regulation has simply gone too far and is past the point of where the costs are being justified by the benefits.

WT: Let's move on then to your time at the SEC. Tell me how that opportunity came to pass.

TP: I was at Wash U at the time, and I received a phone call from the Office of Presidential Personnel asking me if I was interested in being considered for the seat that was going to be opening up when Commissioner Atkins left. I said, "Yes, I would be interested in being considered," and that then launched the process as to myself and whoever else was being considered. That then ultimately was the very first steps that led to my being nominated to be a Commissioner.

WT: Could you tell me a little bit about the nomination confirmation process? How did that go for you? Who did you meet within the executive branch, et cetera?

TP: I met a number of individuals in the executive branches as they were working through their vetting process. Then, once that process worked its way through and then you have the formal nomination, then of course you have your hearing on the Senate Banking Committee. I think as is normal course, there were a handful of senators who wanted to meet as part of their consideration of myself, and I'm sure the others had similar

experiences. So, I met with a handful of senators, and then ultimately the hearing in front of the Banking Committee, and then you wait.

WT: Tell me a little bit about the atmosphere of the Commission when you came out of it. Of course, we're in the middle of the financial crisis at this point so that has to affect things, but one of the things I'm interested in is there are a lot of people who say in the 2000s the Commission was particularly divided, that there wasn't a whole lot of comity, and so I'm wondering if that was your experience of things.

TP: I distinguish two things. One, I distinguish the votes from the interpersonal. So, there certainly were a number of three-two votes when I was there, and I found myself dissenting in many instances. And yet, at the same time, while there were obviously, as those votes reflect, differences when it came to policy among the Commissioners, I always found it to be a very collegial group and I truly count everybody that I served with at the time as a friend, and now still as friends.

I think that's important, because, particularly during a crisis, there are very trying circumstances, it's demanding, there are a lot of difficult questions, both as to the crisis but of course the aftermath, the number of the rulemakings that the Commission was charged with. You will have your points of agreement and your points of disagreement on policy, but it's important, at least from my perspective, that it be done in the spirit of collegiality and folks genuinely at the personal level getting along, and that was my personal experience during the time I was there.

WT: Would you characterize the philosophical position—I guess rather than saying necessarily the political positions of the various members—as fairly polarized, or was it a spectrum? Clearly, everyone's not quite on the same page in that respect, but I'm wondering what your perception of that is.

TP: I would say clearly not everyone's right on the same page, exactly the same page, but one wouldn't, to your point, expect that given the nature of the structure of the Commission in terms of being politically divided. You're going to expect to see some of those differences on philosophy, differences on policy. I certainly don't want to characterize my colleagues' views or where they would maybe put themselves on the policy or philosophy spectrum.

But what I would say is, if you have five individuals, you have the backgrounds of the five who were there when I was there, or any of the five who happened to be there when I was there, there were some different blends of five: you bring your philosophy, you bring your policy views. But, in addition to that, everybody brings their own experiences, and their own approach, and their own way of coming to the job. There's no single way to do it. So, because of that, when you think about those differences and those different dimensions, you're going to get five folks who are coming at it with their independent perspectives, offering what they offer, and you see where you land. And whether that's a 5-0, a 4-1, a 3-2, or who knows what, it's not always going to be straightforward. But I

don't think the structure of the Commission anticipates that it's always going to be straightforward.

Again, once you realize that it's politically divided by statute, and once you realize that things—at least at the policy-making levels, say the rulemakings, for example—things require three individuals to support something, and sometimes you only get three, sometimes you get four, sometimes you get five. But everyone, again, is going to be bringing something different to the table beyond differences of philosophy and policy, simply because everybody's had a different set of experiences that they offer up and that's going to inform how they approach the issues in front of them.

WT: One thing that people from earlier periods who are with the Commission, both as Commissioners and I think as staff, have commented is the actual use of—I guess, in the Supreme Court they call it a dissenting opinion; I guess you just call it a dissent in this case—was that something that was regarded as novel when you were there?

TP: There had been some dissents, published dissents, before I got there. So, when I dissented it certainly was not the first time a Commissioner had dissented, nor was it the first time that a Commissioner had dissented and expressed it in a written dissent. So in that sense it didn't strike me at least as being out of the norm to issue a statement. To the contrary, my view was—and frankly continues to be—that regardless of how I was going to vote on something, whether it was for or against, that it was important for me to explain my thinking so that interested parties had an understanding as to not just where I

came out, but why I came out the way that I did. Those who were interested might agree with me or they might disagree with me, but I thought that folks should understand my thinking as to why I landed where I did. The best way to do that is, from my perspective, in the context of writing it up, and if you're voting no, that takes the form of a dissent.

But every time I voted yes for something, I of course—maybe not every time but almost every time—I wrote a statement as well. Now, in some instances it might have been more straightforward, so there wasn't quite as much to say. But, in other instances, even when voting in favor of something, oftentimes there was something in particular that I wanted to single out and explain in terms of how I was thinking about it. Those statements provided that occasion.

The other occasion to express yourself is speeches and conversations and fireside chats. I do think that sort of communication with the public and with interested parties, to my mind is important, so that individuals understand where those who are voting on these really important matters—how they approach these topics and are thinking about these topics. I think that's important.

WT: Bring us in now, I guess, to August 2008 and what the state of affairs is. Already the financial crisis is underway. I think it was in September that Lehman declares bankruptcy, so that hadn't quite happened yet. So it's really in the thick of things.

TP: It is the thick of things. I got sworn in August 1, 2008, and just about a month and a half later we have all of that that the middle of September brought. It was a very challenging time, as we all recall. And, from my perspective, you've been there all of six weeks and you find yourself in the middle of the greatest financial crisis since the Great Depression. It was challenging, it was humbling, it was demanding, and yet sitting there just as an observer was certainly not an option. The SEC had its responsibilities, other parts of the government had certainly their responsibilities, and everybody was paying careful attention.

WT: What was it at this point that the SEC was able to do? Of course, the Fed takes a very prominent role in all of this because it has the checkbook, so to speak. What was the role of the SEC in all of this, or what did you perceive its role to be?

TP: One of the most notable things that the SEC did was around banning short-selling in financial services stocks, and that got a lot of attention. It turns out, with retrospect, it didn't seem to have the beneficial effect that one might have hoped for. But, of course, it was not a permanent step.

It was something where in February 2009, at the first SEC Speaks event where I had the chance as a Commissioner to speak, I spoke about my thinking around the decision to put that ban in place at that time, under those circumstances, and then ultimately I used that as an occasion to talk more generally about cost-benefit analysis. One of the general lessons that I pointed out—and this is something that carries forward during periods of

turmoil as well as periods of calm—is that, whether you’re a policymaker or you’re in the private sector or the academic sector, the fact of the matter is you’re challenged with making decisions and you’re never going to have perfect information. In some instances you won’t actually have a whole lot of time, either. I think that really captures where a lot of folks found themselves during the financial crisis—whether in the government sector or in the private sector—where a lot of decisions had to be made. There wasn’t as much time as anybody would’ve liked, and there wasn’t perfect information because of that. Yet sitting by and doing nothing is not an option, and the way to think about that is doing nothing is itself even a choice. So you do the best you can.

I think what’s important, in addition to doing the best you can, is that you learn from those experiences. That’s the case, again I would say—not just when it comes to steps taken during a period of turmoil, but during every period—is that you do the best you can in anticipation of what’s going to come. But at some point you actually see what the result is, and learning from those actual results and taking a look back and trying to learn lessons about what you did that was right and what you did that maybe missed the mark, so that next time around you get the benefit of that experience.

WT: What kind of pressures did you and your fellow Commissioners—Chris Cox was Chair at the time—experience from Congress, from the executive branch, from even the press to do “something,” or to take particular actions?

TP: One of the areas, just to make reference to it, is there were a lot of folks who were of the belief that short selling was a contributing factor in terms of driving down the price of stocks, which would then have the follow-on effect of further eroding confidence, which would have a follow-on effect. Then you have this set of cascading effects that, if not of precipitating events, could be a contributing factor. This was getting a lot of discussion, at least as my memory serves, in a lot of different quarters.

So, whether one thinks about it in terms of pressure or not, I think about it more in terms of when you sit back, and there are thoughtful, experienced individuals pointing out something that you think is making things worse, you take that to heart and you think about it, and then you ask yourself, well, what might you do and what are the costs and the benefits of taking a step, and that was my simple framework when thinking about what to do when it came to short selling. I think whether it's in the context of a crisis, though, or some other period, I think ultimately the charge is to do what you think is right.

WT: Of course we're in the middle of an election cycle at the same time as well, so there's a bit of uncertainty not only as to who's going to be in there but what actions whoever wins the election, be it John McCain or Barack Obama, what actions they would take. You've heard some people say that, "Well, would the SEC even survive?" or maybe a little bit less radical, "Would the SEC be merged with the CFTC?" How much genuine uncertainty was there in what the future of the legislative and institutional future hold?

TP: There certainly were a lot of criticisms leveled at the SEC at that time. And there was the questions of whether, as you said, “Should the SEC continue to exist or should it be merged with the CFTC?” or just an overall restructuring of the financial regulatory architecture beyond the substantive regulatory regime, in terms of the government bodies that would be doing the regulating. Those were all discussions that were taking place, that had been taking place. It was very difficult to know for sure in the middle of it how anything exactly is going to play out. I’m not sure, as I think back on it now, that I personally would have placed a high likelihood on the SEC going away. Yet, at the same time, there were lots of discussions which were playing out in the backdrop, at least to a degree, if not in the foreground.

I think when it comes to the substantive response, the legislative front—to the extent history is a guide here of when you have something like the financial crisis of 2008—you get a legislative response and a regulatory response. Now, what that was going to be exactly, well, to your point, that would turn at least in part on what would happen in the election and who would be in control of the White House. But I didn’t have personally much doubt that there would be some sort of regulatory-legislative response, but to know exactly what it would be was hard to predict at that point.

WT: How quickly after 2009 started—Mary Schapiro comes in, you have the new President, the new Congress comes in—how quickly did the shape of things come to look like the process that eventually brought us to Dodd-Frank?

TP: I don't recall off the top of my head, in terms of how quickly that process kind of told us what Dodd-Frank was going to look like. But, if you think about when the President came in, and then you think about when Dodd-Frank was enacted, and you think about the initiatives that Senator Dodd was pushing forward and those that Frank was pushing forward, just the basic contour started to take some shape. What you ended up seeing, though, of course, is a piece of legislation that addresses a whole lot of things, some that have some connection to the crisis and many things that seem not to be particularly connected to the crisis. All of that is setting to one side what one's views are of Dodd-Frank as a whole. But there ended up being a lot in Dodd-Frank, as this process played itself out and as things got added, that if one was, I think, thinking about a legislative response to the crisis, one probably would not have anticipated it being the final legislation.

WT: Let's talk a little bit more about the cost-benefit analysis aspect of things. I was speaking a month or so ago with Erik Sirri, so he got into some of these issue in some detail. At this point you've had, I guess, the *Chamber of Commerce* case that overturned the rules on mutual fund governance. I think that's correct. So, this is already something that's on the agenda. According to Erik, there wasn't a terrifically well-defined procedure for cost-benefit analysis. Was that your perception when you came in?

TP: In addition to expressing concerns in speeches, particularly post-Dodd-Frank, about overregulation in just about every speech, I think in just about every speech maybe from the very beginning I expressed my belief that much more needed to be done by way of

rigorous cost-benefit analysis. And that reflected my view that the agency had room to improve on that front.

And I'll say—we can go back and unpack this some—but the agency has made significant strides over the last two or three years in particular, in terms of more economists inside the agency, in terms of the economists being much more integrated throughout the rulemaking process, the regulatory process generally, a much greater focus on data than had been the case historically. So, while I think that, as I said, when I arrived the Commission had a long way to go, I think it's positive that the Commission has made meaningful and notable strides. My hope is they'll continue on this trajectory and that it has not plateaued, and that economic analysis and cost-benefit analysis will prove to become increasingly second nature and part of what the agency does.

The reason for that is simple. Going back to what I said in terms of my being an economics major and my introduction to economics, is—regardless of one's policy view on a topic, or one's philosophy overall of regulation, government, of markets, however you want to think about it—is that the overall call of cost-benefit analysis is to try to put decision makers in the best position possible to understand the possible consequences of their decisions, to try to make sure that when you make a decision you are as able as you can be to understand what's the good that could happen and what's the bad that could happen. So then you can make an informed trade-off, because policymaking, regulating, is ultimately about trade-offs -- am I willing to trade this outcome against that outcome.

Without understanding what those potential outcomes may be, you may find yourself making a decision that, had you had more complete understanding, perhaps you would have made a different choice. Cost-benefit analysis is that discipline, is that exercise in economics, in addition to all the other skills that the Commission and the staff bring to bear, rounds out the understanding and makes sure that you are more likely to spot the range of possible outcomes so you can have as an informed a decision as possible.

WT: How deeply at the Commission level would you have been engaged with the questions of methodology of cost-benefit analysis? Of course, on the cost side, a corporation would require x number of lawyers, y number of accountants, and so forth. It's fairly easy to—well, I don't want to say easy—but there's a certain quantification that can take place there. In terms of benefits, those are oftentimes a little bit more hazy, “How do we head off systemic risk in the broader economy?” How are those things taken into account and to what degree was that considered at the Commission level?

TP: I think it's all taken into account that, to one degree or another—this goes back to the point about trade-offs and the policy choices one's making—or I should say I hope it's all taken into account in terms of how these choices are being made. But, when you think about the difficulty in some instances of quantifying a benefit, or quantifying a cost, some things are able to be reflected in a number. But part of this, when we're thinking outside of that which you can quantify, is trying to understand what does one really think the behavioral consequences are? What does one really think is going to be the ways in which this changes the way things get done in the private sector?

And so, when you think about behavior, you think about some basics of game theory, you think about, well, how is this actually likely to really in fact play out and is that what we want to have as a consequence, or not what we want to have as a consequence? A lot of that rigorous qualitative analysis proves to be particularly important as well. If you have that rigorous qualitative analysis around, what one thinks the impacts of a rule are likely to be and how you think about that in terms of cost-benefits, it really challenges one to assess in a very rigorous way. If we put this rule change in place, are we really going to be achieving the outcome we want? That's in addition to understanding what the cost of compliance may be.

And oftentimes what you may find out is that the changes in the marketplace that a particular rule is likely to bring about, maybe it'll bring about some changes that we actually like. But there's a really good chance, if we think this through, that it's going to bring about some changes that actually we don't like so much. We can put that in the cost category, and, as you net it all out, the question then is, is this worth doing or not, or is there a different approach? So that's the way, at least for me, to think about it. It's both that which you can quantify, but I think also the rigorous qualitative analysis, as you try to think about, in very simple terms: how is this likely to play out in fact, in real life, this rule change, and is that what we want or is that actually not what we want, in which case we need to go in a different direction.

WT: You can see it as almost a broader policy analysis rather than as a cost-benefit analysis,.

TP: I use the “cost-benefit” phrase for a lot of reasons, but another way I often put it, and would express it in speeches, is it’s really trying as best I can to understand consequences. You can think about it as a cost-benefit analysis—and I do think about it that way and I do think that’s a proper way to think about it—but to take a step back and say, “All right, help me understand what the potential consequences are of this rule change or that rule change.” I’m going to categorize some of the consequences as good, and we can call those benefits, and some of those consequences as not good, and I’m going to call those costs. Then I’m balancing, because, again, I think when it comes to just about any regulatory change, when you undertake that analysis there are going to be some things you can anticipate that you would say, “Yes, that’s a good change.” There are other things that you can anticipate and you can say, “Well, that’s not what we want.” But that’s always going to be something that we’re presented with, things we like and things we don’t.

The question then becomes, how do we trade those off? That’s the ultimate challenge of policy making. You come back to the basic structure of the Commission, and you’ve got five individuals with their own perspectives and philosophy and views and experiences. They’re going to make different trade-offs from time to time, and I think that’s what you see oftentimes as being reflected when you have split votes in the Commission.

WT: So, insofar as this capability develops in the Commission in this period, how much of that is concentrated in this new Division of Risk, Strategy, and Financial Innovation that gets established around this time?

TP: And now it's DERA, right?

WT: Now it's something different.

TP: So, you had the Office, then you had RiskFin, and now you have DERA. That's, if you will, the core of it, but as you look across the agency there are folks with this kind of background of technical economic skills, and Ph.D economics and quantitative skills, as well as folks from industry who can add a richness to the analysis as well, particularly as you're trying to anticipate how things may play themselves out. While DERA is a centerpiece of that, there are folks spread throughout the Commission who can offer that expertise. And again, as I said, my personal hope is that the agency over time continues to develop those resources, because I think it just puts the Commission in a much better position than would otherwise be the case to anticipate what the implications would be of particular rule changes. Or frankly, from that perspective, it can also help the Commission better anticipate points of risk and concern sooner than might otherwise be the case. So, it serves those beneficial effects as well.

WT: Previously there had been the Office of Risk Assessment, and I gather that this was not a very large affair in the late 2000s. Could you tell me what that looked like before the new division came in?

TP: There was the Office of Risk Assessment, and then there was the Office of Economic Analysis, and I think there was an Office of Risk Assessment and an Office of Economic Analysis, and then you got RiskFin and DERA. So, again, I think a way to think about it is that there was the increased commitment to this function within the Commission. It went from office to division, with some changes to some degree around the division between RiskFin and DERA. But it is, again, a reflection of the commitment more than had been the case in the past that this sort of economic analysis and data-driven analysis is key to the Commission.

And, candidly, I think in no small part, it's probably fair to say that a prompt to that change and perspective overall is a function of the fact that the Commission was having challenges in the D.C. Circuit, and then having had rules overturned for not having adequate cost-benefit analysis, and therefore having APA [Administrative Procedure Act] shortcomings. And so, after a series of cases where the Commission was having its rules overturned, I think that was precipitating a series of events that caused a change in approach in terms of a commitment to economic analysis at the Commission, and I think that's all for the good.

WT: So, aside from the financial crisis, there's also the Madoff scandal that comes up and is accepted to be a real black eye for the Commission. What did the conversations surrounding that particular event look like?

TP: As you said, it was a tough time for the Commission. There have been a number of reports and analyses after the fact dissecting the whole scenario, so leave those be. But I think one of the effects, that's kind of an institutional effect, is the Commission was coming under a lot of criticism from a lot of quarters for a lot of things, and that can have an effect on any organization.

If you think about overwhelming the folks at the Commission who were working extremely hard, making a lot of sacrifice, working very diligently and earnestly, it was a very tough time for a lot of folks to be at the Commission. The Commission went from being the agency that was held up as the crown jewel of administrative agencies, to being criticized by a lot of different quarters for a lot of different things, and so that has an effect.

As I said—and to the credit of staff and folks at the Commission that continue to keep their head down, who did at the time, and do their work—I think the Commission has demonstrated, going back to the point about economic analysis, some real kind of improvements in terms of how it does what it does as a general matter. I think if you take the Madoff experience and other experiences, thinking about how the Commission could improve itself in various ways from a lessons learned perspective, and so there's been a

lot that's come out of that, arguably for the good. But it was a tough time for the Commission.

WT: Let's talk specifically about the discussion surrounding enforcement policy. I gather that there were a few things that were done in this period to adjust some of the criticisms that were made. For example, the enforcement division got the authority to—the term is escaping me just now.

TP: Formal order authority.

WT: Yes, the formal order of investigation. Could you tell me a little bit more about what was going on as far as the discussions around enforcement were concerned?

TP: When it comes to enforcement generally, there have been over the last handful of years a number of changes that have been brought into effect. You made reference to one, their efforts in terms of cooperation, to try to encourage greater cooperation from those the Commission may charge. There's a change in the neither-admit-nor-deny. There's Chair White's initiative around so-called broken windows. We could go on and on in terms of specialized units, on and on in terms of changes that have been ushered in over the last handful of years.

One of the things though, for me, which I talked about when I was at the Commission, one of the tough challenges is trying to evaluate what cases to bring, what cases not to

bring, who to charge, what theory, what sanction and all the rest, where you have to think about, at least from my vantage point, the opportunity cost of your time and effort and your resources.

A point I used to make when I was at the Commission in speeches is that it's important to think about opportunity costs. It's important to think about, if one pursues Case A with all that you got, that may take resources away from Case B, and it turns out Case B may be a better case to pursue. How do you allocate your resources the most efficiently and effectively across the portfolio of different things that one could pursue from an enforcement perspective?

When you think about that, sometimes the best decision—I underscore sometimes—is to not pursue a particular case because it frees up those resources to be dedicated towards more impactful cases that should be investigated. Yet that can be a challenge. I do think it's an important consideration that is something other than all of the various initiatives that have been put into effect that needs to be thought about, the importance sometimes of not pursuing a particular case so that those resources could be dedicated to other cases. And for the staff and others to realize that the tough decision to not pursue something is something that is rewarded and valued, because it allows those resources to be, again, dedicated towards other matters where it may be more impactful to commit the resources.

WT: In the aftermath of the financial crisis, what enforcement options were particularly available? I mean, in many ways it's an economic/financial problem rather than a

problem of malfeasance. There are instances, such as with option rate securities, where they were marketed as essentially a cash-like instrument, overstating liquidity. But to what degree was there room to take enforcement action in that milieu?

TP: Well for me it's pretty straightforward in the following sense, that it comes down to facts, and it comes down to the law, and that when it comes to enforcement that one can't bend to political pressure or public pressure or anything like that. It has to be the law; it has to be the facts. When it comes to the law, you can pick whatever provision one wants under the federal securities law, they each have their elements of the offense and you have to march through element by element.

If the law and the facts substantiate a case, then you have a case. I think you still, to my prior point, need to make a decision as to whether or not the commitment of resources to that particular matter is the highest and best use of the agency's resources. But if after you do the analysis where you apply the law rigorously to the facts, if it turns out there's not a violation of the federal securities laws then there's not a case, and it's pretty straightforward in that respect. That's the way it ought to be and needs to be, from my vantage point, whether we're talking about the financial crisis or otherwise, and that's an important kind of bedrock for me in thinking about enforcement.

WT: In terms of the size of penalties, this gets to your interest in behavioral responses, there's a lot of calls to increase the size of penalties because that will give the regulations more

teeth, so to speak. Was that your perception? Was that a viable remedy in this time period?

TP: One of my concerns - that has been expressed by others - is that when you impose large penalties, certainly if you impose large penalties on corporations, the cost is ultimately being born by the shareholders of the company. I think the analysis becomes more complicated when one's thinking about imposing a large financial sanction on an entity, in terms of the question of who is ultimately bearing the cost.

The other point, which is very much related and individuals other than myself make, is that it's the individuals who act, as compared to the entity. It's the individuals within an organization who are the ones who are engaging in the misconduct, to the extent there was in fact misconduct engaged in, and that it's important to hold individuals accountable.

Now, what I would be quick to note there is that insofar as there is a focus on holding individuals accountable, it's important not to stretch to hold individuals accountable, like going back to the prior point of whether it's as to individual or if one is charging an entity, that it has to be a straightforward, balanced, rigorous analysis of the facts and the law. If the facts and the law justify bringing an action, they do, and if they don't they don't, but that one ought not stretch to try to bring somebody within the scope of the law if their activity in fact falls outside, or if the facts simply don't meet the elements of defense.

WT: The other gut response people have is “Throw the bums in jail.” Of course the SEC does not have the authority to throw people in jail or to engage in criminal prosecutions, but it does interact oftentimes with the Department of Justice, with state prosecutors, attorneys general. To what degree was that part of the equation trying to enforce the marketplace?

TP: There certainly are other parts of the government, as well as private litigation. You could have something that is not a violation of the federal securities laws. It doesn't mean that that activity didn't violate some other body of law, or give rise to a cause of action that's simply outside of the scope of the federal securities laws.

In other instances, you could have a violation that could both give rise to an enforcement action by the SEC, as well as to prosecution by the Department of Justice, as well as give rise to private litigation. The legal construct anticipates that you may have multiple causes of action by multiple parts of the government, as well as private parties. But again, I'll go back, at the risk of still repeating myself, that this all turns on the law and the facts and can't turn on getting into pressure to bring action, or to bring your prosecution, if the law and the facts don't substantiate it.

WT: So now let's go to the Dodd-Frank legislative process. First, to what degree did the SEC have input to that process? I was talking to David Becker and he felt that it was perhaps a bit of a spectator sport for the SEC, given the role of the Fed, but I'm not sure if that was a widely-held opinion.

TP: I think for me personally, and I think this may be a function of the way things—it's a piece of legislation that was largely being supported by a particular party at the end of the day, so I personally was not closely involved in the development of Dodd-Frank. I can't speak for the ways in which others may or may not have had been more closely involved, but for myself I was not closely involved in the creation of Dodd-Frank, and that observation is perhaps consistent with what I said before about most of my speeches post-Dodd-Frank, expressing a lot of my criticism of the legislation.

WT: So let's talk, then, about specific things that the SEC was supposed to participate in. As early as 2006, you'd had legislation over credit rating agencies, but I gather that the rulemaking surrounding that was still going on. Could you tell me about that?

TP: The rulemaking is still going on in the Commission, and it did still rulemakings under the 2006 legislation, and then recently, after I've left, completed rulemakings under Dodd-Frank. So, there were the 2006 rulemakings that were to be completed, and then there were the Dodd-Frank rulemakings that the Commission finalized not so long ago.

WT: Could you tell me a little bit about what these rules were expected to accomplish? What your own opinions of them were?

TP: The rules try to get at concerns that folks had around conflicts of interest, for example, as well as more disclosure so you can have more market-based accountability in terms of the

evaluation of rates. So, you have the 2006 legislation, which, again, put into place a number of requirements of rulemakings, and you have the Dodd-Frank legislation that provides for a host of rulemakings, but conflicts of interest is something that has been an area that's been a focus of a lot of attention when it comes to ratings, and again, a lot of regulatory change in that regard.

WT: One of the goals in the 2006 legislation is to create more competition among rating agencies, which would hopefully spur more innovation, which I suppose is one of these behavioral questions that you're interested in. Could you talk about to what degree the rationales there were sound or not sound?

TP: Well I, as a general matter—and again speaking as a general matter—think that competition can go a long way in terms of disciplining behavior and giving investors choice and consumers choice as well as disclosure. So, when you have choice and when you have disclosure and you have competition and you have investors in a position to make informed decision making that that can generally be, or often be, a very effective alternative as compared to a more substantive, one-size-fits-all regulation from government.

WT: Money market funds, tell me about some of the discussions that were had around those. I guess there were questions of regulating their contents versus the possibility of going to a floating value for them. What were the options there?

TP: There were a number of options. Where the Commission ultimately landed is a combination—well, it's complicated, so I'm just going to say there were fees and gates, but also a floating, maybe, for certain funds, without getting into all of the particulars. I'm personally on record through various statements at open meetings and otherwise of having not supported floating the NAV, and yet the Commission has a floating NAV, has fees and gates as part of the final rulemaking. Again, there are different requirements for different types of funds, but a lot of the focus has been centered around whether or not the NAV should be floated, and that was something where there were strongly held views around that issue. But the Commission ultimately worked its way through and put in place the final rules a while back.

WT: Then there's this question of capital requirements, and I know that one of the issues that you've been concerned about in your speeches is the question of capital formation, whether this will be hindered, and I know that these two points are considered to be in conflict.

TP: I think there's a couple points. One is if you think about capital requirements generally, as compared to capital formation, so the common point there is capital. But one of the concerns that I've had with capital requirements is just—again, it goes back to the point about cost-benefit analysis—is as you put more and more stringent capital requirements on financial institutions, there's going to be at least to some degree less capital out circulating in the financial system and doing all the work that capital does, and it can be

put to other uses and that comes out of cost. Again, this is a question of trade-offs, and people are going to make different judgments about that from time to time.

When it comes to capital formation, and spurring and facilitating capital formation as a way for businesses to be able to get the capital they need to grow, to invest, to hire, to prosper, I've been a proponent for a long time now of the Commission taking more positive, proactive steps to try to spur capital formation, to try to spur the ability of companies, particularly small companies, but all companies to get access to the capital they need to grow. I think that's consistent with the Commission's mission. It's good for overall economic growth and prosperity, but I think it's also good for investors when investors have that many more opportunities for how to put their money to work.

The other side of capital formation, the other side of companies raising money, is investors have the ability to invest in those opportunities. So, there's an opportunity not only for issuers and their enterprises to be better off, and what that means for our economy, but also opportunities for investors to have more things to invest in, and that gives them the occasion to build wealth and earn income and have greater financial success than might otherwise be the case.

WT: One of the chief criticisms, in terms of diagnosis of the financial crisis, is that there were regulatory blind spots. Over-the-counter derivatives was, of course, an essential one, but also particular gaps in capital requirements that allowed banks to become over-leveraged. Was it your perception that those contributed to the crisis, and is it your perception that

those were, in fact, key problems for regulation that needed to be addressed in the aftermath?

TP: One of the things about the crisis is I think there's still going to be time for folks to diagnose what the full set of causes of the financial crisis were. If one thinks about it in terms of housing policy, for example, then that would be a root cause. If one thinks about it in terms of some other factor, then that would be another root cause. I think to lay blame at, say, the over-the-counter derivatives market as being the cause of the financial crisis, I wouldn't put myself in that particular camp.

To the extent there are some changes that have been put in place to some degree that make some positive contributions in terms of the regulatory regime, we'll see ultimately as things play themselves out on the cost-benefit front what the net effect of, say, Title VII is. It's a brand new regulatory regime. The SEC has a piece of it. The CFTC has the larger piece of it. One of the things that I would caution is, as that regulatory regime gets put into place fully and completely, and it has been up and running for some time—

WT: This is the OTC derivatives?

TP: –Yes, that regulators take a step back and look at that regulatory regime and see how it in fact has played itself out. Because I think any time you build a new regulatory regime from scratch, there's some opportunities to miss the mark, notwithstanding what may be the best of efforts.

WT: I know in some of your speeches you've been quite critical of the Volcker Rule, and in particular trying to apply it to the regulation of certain activities and not others. Maybe you could talk a little bit about that particular problem as it pertains to the SEC.

TP: Yes. The primary concern there was, at least for myself, is that what you're going to have is you're going to have an undue crimping of market-making activity. I still worry about that, whether, as a function of the Volcker Rule or as a function of increasing capital requirements, for example, the ways in which that can restrict the kinds of activities that financial institutions participate in and how it can actually have adverse consequences for the marketplace.

It comes back to this point about root causes. If one believes that proprietary trading was a root cause of the financial crisis, then you can see how one may call for the Volcker Rule. But, if one does not think that proprietary trading was a root cause of the financial crisis, then the benefits of the Volcker Rule are going to be suspect. If you think that market making is particularly important to the financial system and potentially crimping market making as one tries to draw this distinction between what's prop trading and what's market making, it means that there's a real chance that the Volcker Rule comes at a very high cost.

WT: A lot of the questions surrounding what regulations are and are not appropriate seem to revolve around the question of liquidity. And so there are certain things like market

making, like short selling, like flash orders, that, for the benefit of them, this puts additional liquidity in the market. But then there's the concern that liquidity suddenly dries up on account of failures within these things. To what degree is that central to the thinking on what does and does not constitute beneficial regulation?

TP: When you're thinking about market structure and liquidity and the way our markets are performing, and our equity markets, I think it's important to let the data drive the analysis and to think about where we are today versus where we were ten years ago, fifteen years ago, maybe even five years ago, whatever period of comparison one wants to undertake. I think it's also important to recognize that whenever one tries to micromanage the structure of a market, at least from my perspective, there's a significant risk of unintended consequences actually making matters worse and not better. So that's an overall kind of framework for me when I think about the approach to market structure and the SEC's regulation of the markets.

I think another possibility—particularly at this point, where there a lot of different trading venues for investors to transact in—one way to think about that is there is in fact a lot of competition. So, in a market where there's a lot of competition and a lot of choice, does that argue for a different role for the SEC as compared to a much more regulatory stance that the Commission's taken now for several decades. I think that there are some real fundamental questions to think about when it comes to the approach to market structure. But I think at the backbone of all of it is not losing sight of the data, and a recognition as the SEC, if it were try to come in and further regulate the micro-market structure, that

there is a real risk that things could actually be worse as a result of unintended consequences as compared to, on net, better.

WT: The role of technology, in particular automated trading is central to the question of market structure. To what degree was and is the SEC equipped to handle the specific questions that come up around those aspects of market structure?

TP: The Commission now, with the individuals who are there, is increasingly well-positioned to be able to access the data, crunch the data, understand the data, which is not to say there haven't been really high-quality individuals at the Commission for a long time. There have been. It's a matter of more folks who can focus on these issues and whose task it is to in fact focus on these issues.

So that's to say that the Commission, I think, is in a better position than it has been in the past to do the kind of data-driven analysis, to focus on the economics, than would have been the case before, by virtue, if nothing else, of the sheer number of individuals it has committed to these, and some of the commitments when it comes to the technological and other tools that the agency now has at its disposal, so it can actually crunch the data and understand in ways that, without a data-driven approach, you simply wouldn't be able to.

WT: One of your central interests, as you mentioned before, is governance. I know in the late '90s and early 2000s, governance was at the center of some of the key initiatives of the

Commission: auditor independence, the independence of mutual fund board members, and a couple other issues as well. To what degree do you see rulemaking surrounding governance as being an effective tool?

TP: When it comes to governance, I've been an advocate of private ordering as compared to one-size-fits-all mandates, and so I've generally not been in favor of the federal government trying to dictate governance structures as compared to allowing companies flexibility to come up with the governance structures that best fit them.

From that vantage point, I can think about various speeches or various rulemakings, where on those very grounds I dissented from things that the Commission did expressing favor for private ordering. Private ordering is something that you see reflected in a state law approach to corporate law, as compared to the federal approach to these topics, which tend to be more one-size-fits-all mandates, which again, as I said, my favor is towards private ordering approaches.

WT: One of the provisions of Dodd-Frank dealt with proxy access, if I'm not mistaken in particular, I believe concerning the election of board members. What was your take on that?

TP: I dissented from the mandatory element of 14a-11. I didn't express dissent when it came to 14a-8. The 14a-8 approach was a private ordering based approach; 14a-11 was a mandatory approach and I dissented, largely for the reasons I just mentioned, in favor of

a private ordering approach as compared to a one-size-fits-all, plus a general view that these questions of governance ought to be addressed at the state level as compared to the federal level.

WT: To what degree were the practices of international markets on the minds of yourself and the other Commissioners in this period, particularly the pressure that people would seek to raise capital on those markets rather than the American ones?

TP: It's certainly on my mind in terms of thinking about the competitiveness of the U.S. marketplace and thinking about the ways in which capital can flow well. So, thinking, frankly, about the ways in which individuals are increasingly willing to relocate elsewhere as well, I, as a policymaker, and I think others, need to take that into account.

In part, it speaks back to this question of what are going to be the actual consequences of putting a particular regulatory change in place. If you think about a regulatory change you want to put in place and subject that activity or those institutions to some type of regulation, but if that activity and those institutions decide to go elsewhere, then, have you really achieved your goal? Whereas, if you subjected them to a somewhat more, perhaps focused scale-tailored regulatory requirement, maybe they'd actually continue to transact here and be located here in the U.S. as compared to going overseas

Things like that need to be, at least in my mind, thought about and taken into account when one makes their ultimate policy judgments. But bottom line, I worry a lot about the

competitiveness of the U.S. markets and capital flows and what that then meant for what the proper regulatory regime was here in the U.S.

WT: On a similar topic, you mentioned the JOBS Act quite a bit earlier, and that comes along in your period on the Commission. I gather that, in general, you approve of that.

TP: Yes.

WT: What are some of the considerations there, in terms of finding a balance between investor protection and raising capital?

TP: I'll go back to what I alluded to before, that oftentimes there is this either/or that's presented, that either you can go capital formation, or you advance the goals of investor protection. I actually see it quite differently, that promoting capital formation is entirely consistent with investor protection, insofar as what investors are most interested in. I think overall is the chance to accumulate wealth, earn income, find financial success, and what that means is opportunities for putting their money work, and the more opportunities investors have, I think everything else being the same, the better.

Now, of course, you need to adequately protect investors against abuse, fraud, misconduct and the like. But there is the prospect for regulation to simply go too far, to be too prescriptive, to be too burdensome, to be too costly, not just measured from the perspective of issuers, but also measured from the perspective and seen through the eyes

of investors themselves when they find themselves denied certain investment opportunities that would be legitimate investment opportunities but the regulatory regime was simply too burdensome for those enterprises to be able to raise capital, to go public, or to otherwise invest and grow.

I don't view it as either you promote capital formation or you advance the interest of investor protection. As I said, I think, in important ways, promoting capital formation actually advances the interest of investors by giving them more investment opportunities for how they're going to put their money to work.

WT: A couple of controversial issues on the Commission that were part of the Dodd-Frank legislation—I just would be interested in your opinion of them. The first was hedge fund registration. I gather that that was a very contentious set of debates, that there were a lot of comments received that were very much against that.

TP: The question of hedge fund registration certainly pre-dated Dodd-Frank, so now you have hedge funds subject to a registration requirement. There were folks, when it came to the earlier effort—which of course was before I got to the SEC—who took different views as to whether or not hedge funds should be, in effect, subject to the registration requirements by getting rid of certain exemption under the federal securities laws that meant they didn't have to be registered. But that exemption was gotten rid of, and so in substance, the debate resolved itself by virtue of a change in the law.

WT: And then the other one is executive compensation disclosure. I know that there were a lot of strong feelings surrounding that as well.

TP: There are a lot of feelings surrounding executive compensation disclosure, and those are rooted in a couple of different things. One is to what extent do some of the disclosures actually speak to information that's important to investors making decisions, or is it about trying to advance other social goals that some see as falling outside the scope of the federal securities laws.

In another respect, one can think of executive compensation disclosures as speaking to questions of corporate governance as well, that perhaps in some instances may not always fall squarely within what the federal securities law should be oriented, depending upon what the disclosure is. The SEC has a long history of requiring disclosures around exec comp, so we can speak generally, but there are some different aspects that would seem to implicate governance concerns that some may think fall outside the scope of what the federal securities law should be oriented to.

The third concern that's been expressed is that in some of these exec comp disclosures that the cost of compliance may actually prove to be much more considerable than some people anticipate. So, when you take all that together, some of these exec comp disclosure requirements coming out of Dodd-Frank have been somewhat contentious, and we'll see where the Commission ultimately lands.

WT: This question is more or less filed under miscellaneous, but I know you've spoken in favor of the simplified disclosures and statements that I think the Commission considered in 2008, and then there's also this model of click down to get more information. I'm wondering if you could discuss those more general issues of how disclosure is presented to your different kinds of investors.

TP: This goes back to what I was saying before about information overload in my academic work. The Commission has ongoing right now an initiative on trying to rethink and improve the effectiveness of disclosure, disclosure reform, which in no small part is about addressing the information overload concerns. I think finding ways to address information overload is still very important. That could be scaling back some of the disclosure requirements that aren't particularly meaningful to investors these days. It could also certainly mean not adding to disclosure requirement requirements, for information to be disclosed that's not material to how an investor actually evaluates the business and understands the business.

But, setting aside the substantive requirements, which again, I think are important and can be scaled back in some respects, is the question of how the information is presented. I do think there's an opportunity for the Commission to make greater use of technology by way of layering, for example, that could make means for improvements in terms of the accessibility and the understandability of the information that is disclosed.

I would note, I think in some sense, the Commission. at some point down the line—I’ve said this in different settings—may find itself facing a more profound challenge when you think about the ways in which a junior higher or an elementary school student or whomever at that age, how they access information and their expectations. You think about a lot of individuals these days, the way they access their information is on their mobile device, it’s on their smartphone, the way they focus on information is something that is 140 characters or otherwise brief. If that’s in fact the case, when these individuals become adults, what, if any, challenges does that present for how information is presented and disclosed under federal securities laws? Are folks really going to be thinking about reading a 300-page K, or even a 100-page K, or are they going to be thinking about how they can digest and access this information in much smaller, bite-size ways. I think it’s an interesting question in terms of how will individuals access and retrieve information, whether it’s information provided to them or information they go and get, how that’s going to create certain pressures and changes for how information is delivered under the federal securities laws.

WT: Speaking generally or philosophically, what’s your opinion of regulations that differentiate between products that are appropriate for a “sophisticated investor” and ones that are more for a retail public, and the different regimes of disclosure that take place?

TP: I think the best approach, generally speaking, is for the regulatory approach to be one of disclosure as compared to one of substantive regulation, or merit review, if you will, that so long as the material information is disclosed allowing investors to decide for

themselves whether or not they want to invest and how they want to allocate their capital is the better approach. It turns out that's actually the approach under the federal securities laws, but getting into the space of saying, "We think this product is okay for you, but is not okay for this person over here," even if everybody's provided the same information, that is, at least sitting here right now, not a role I'd want the SEC to undertake.

WT: So now—coming back up to the general level, kind of where we're at right now, or at least when you left the Commission—your position, of course, is that Dodd-Frank has been overzealous in a lot of ways. There's going to be criticism coming from other quarters—particularly pointing to some of the very large scandals that we've seen in recent years, and some large penalties that have come out of the same—that in fact, we haven't really done much at all to change corporate culture. Or, if you don't want to change corporate culture necessarily, to at least dissuade people from violating the regulations. How do you reconcile those two points of view? Do you view the latter as a potent concern?

TP: I think there's been a huge amount of regulatory change, as I said. My worry was, and continues to be, over-regulation. I think, when you see those different views and perspectives, I think it comes full circle. Different folks are going to have different takes. They're going to have different takes and different philosophies on what it takes in terms of achieving change, and they're also going to have different views on what the role of government ought to be vis-à-vis the private market. I think that when you see these two

different views that are being expressed, I think that's largely where it comes from, and sometimes one just has to agree to disagree.

But I think wherever you come out on those big pictures, just thinking of generalized questions, I think continuing to evaluate along the way. Just as my concern may be over-regulation and somebody else's concern may be under-regulation, again, we may evaluate that somewhat differently, too; what I may consider to be over somebody may consider to be not yet enough and light, is to take a step back and undertake what folks refer to as a retrospective review and say, "Here's what we did, and here's what we thought was going to happen, and here's what in fact happened."

Now, it can be hard sometimes to do cause and effect. Lots of other things are going on other than just regulatory change, but you should learn from the experience the best you can. If it turns out that I, myself, Troy, am wrong, then I'd like to know that I'm wrong and I can adjust my thinking on a going-forward basis about what the role of government ought to be and what the right regulatory response ought to be. If it turns out others were wrong, they get the benefit of the experience and we can all recalibrate and adjust going forward, because whenever we make these decisions—back to the point about cost-benefit analysis—whenever we're making these decisions about what the right policy is, over-, under-regulation, whatever it may be, we're trying to anticipate outcomes.

At some point we have actual outcomes, so can we learn from those outcomes? Are we willing to say, “I did the best I could with the information I had at the time, given my views and my understanding and my experience and my judgment. Turns out things played out differently, so now with the benefit of that learning, I, myself, would make a different decision on a going-forward basis.” I think we all need to be open to that, to be humble, if you will, and to realize that, again, notwithstanding the best efforts and earnestness and trying really hard, sometimes you make decisions that with hindsight you wish you could do over, but it’s important to learn from that hindsight.

The way I put it oftentimes is, “I voted yes for a lot of rules, and every time I voted yes there were good reasons to vote no. I also voted no for a lot of rules, and every time I voted no there would have been reasons to vote yes.” That is simply to say that, no matter what decision you make, there are costs and benefits. When I voted no, the cost of my decision to vote no was potentially forgoing the benefits that my colleagues thought we were going to obtain, and yet I made a choice as to what I was prepared to trade off and what I thought the right thing to do was.

But learning from that experience with the benefit of some hindsight, not that you get a do-over as such, but to say, “Have I learned something about how I think things are likely to play out next time? Have I learned something that otherwise I didn’t appreciate? Is there a blind spot that now I’m open to? Do I need to recalibrate my thinking?” That’s an important thing to do on a going-forward basis, the retrospective reviews and just stopping and reflecting allow all of us to do that. And that’s something, frankly, that I

think is not just about policy making; that's something that applies across everything we do.

WT: In terms of major scandals at large institutions, do you view these as deriving from systemic causes, be it in governance or in terms of what regulations make into an attractive opportunity for malfeasance, or do you view it as something that would be most effectively remedied through better surveillance, more effective enforcement or something like that?

TP: I think it's hard to paint with a broad brush across all of the economy or all of the private sector, even all of the financial sector, that one would have to go instance by instance and view, if you will, the forensics around all of it and try to really understand what motivated somebody to do something or not do something, and a whole host of respects to try to draw on any firm conclusions.

What I will say is, on the enforcement front and speaking generally, that data analytics actually prove to be quite important in terms of surveillance, in terms of understanding, in terms of detecting. And so it's one of the other areas where the Commission and folks at the Commission have spoken quite publicly about this, about the role of data analytics when it comes to compliance and inspections, examinations, but also when it comes to enforcement, because data analytics power the Commission and others to identify things that otherwise would be difficult to identify, if not impossible to identify with human eyes and ears. It allows one to identify things in potentially a much more efficient and

expeditious way, which would speak to how resources are going to be spent across all the different priorities of the Commission.

WT: Would the Commission be able to effectively use additional resources? Say, if there were larger enforcement, or larger inspection groups, do you think that would be an efficacious use of resources?

TP: The Commission's resources have increased a lot over the years. For me, on the question of resources, my first focus has always been on how are the resources the Commission has, whatever they may be, going to be put to the highest and best use? Others will ultimately decide how many resources the Commission should have, but I think thinking about how are those resources going to be put to their highest and best use.

In every instance, you can imagine one more resource being put to a very effective use, and one more resource not being put to such an effective use. So it's this question of use that I find to be, at least in my mind, paramount to the discussion. I think on that front, data analytics and the role of the economist inside the Commission are particularly important to everything the Commission does across all of its responsibilities, both in terms of subject matter areas, but also when it comes to rulemaking, compliance, enforcement and otherwise.

WT: Do you have any additional thoughts about your time in the Commission?

TP: It was a terrific opportunity, a chance to be there at any time, let alone the chance to be there at the time I had the privilege to be there. Everybody says if you serve it's a privilege and an honor, and it truly is a privilege and an honor. I got to meet a lot of interesting people. I got to make a lot of good friends, as well. I have the utmost respect for the staff and my colleagues on the Commission, and it's always the case that I wish the Commission nothing but the best.

WT: Could you tell me just briefly, then, about some of your activities after. I gather you decided not to go back into academia.

TP: I do a blend of things. Most of my time these days is spent in the private sector, consulting on a wide range of relevant topics to the things we're talking about today. I also have a foot in academia with some not full-time affiliations, but some other affiliations. Last spring I was teaching corporate law, and this coming spring I'll be teaching securities law, and still trying to do some writing when I can find the time. And certainly, as we talked about before, I have the treatise.

WT: Well, that pretty much does it for my questions then, unless you have anything else to add. Thank you very much.

TP: Thank you. I appreciate it.

[End of Interview]