

Diane Sanger Memorial Lecture
March 22, 2012

RICHARD NESSON: Good afternoon and welcome to the 2012 Diane Sanger Memorial Lecture, broadcast live from the Georgetown University Law Center and worldwide online at www.sechistorical.org. I am Richard Nesson, President of the SEC Historical Society, which is presenting today's program.

The Historical Society, which is a non-profit organization entirely independent of the SEC, shares, preserves and advances knowledge of the history of financial regulation through its virtual museum and archive at www.sechistorical.org. The virtual museum and archive, which is celebrating its 10th anniversary this year, provides visitors access at all times to primary sources that are part of the history of the U.S. financial regulatory system, including papers, oral histories, photos and film, radio and television media. Through its programs, the museum seeks to contribute to that history.

Our hope is that today's program, examining the survival of investor protection, will help shape the ongoing debate about the proper role of financial regulation. Today's discussion will recognize and further the values that Diane Sanger sought to implement throughout her too-brief life. We would like to thank Georgetown University Law Center for joining with us to present today's programs. Support for the growth of the virtual museum and archive comes entirely from gifts and grants from individuals and institutions. The Society is grateful for the generous gift from the family of Diane Sanger in order to make today's lecture possible.

I am delighted to welcome Bryna Sanger, Senior Vice President and Deputy Provost of The New School, and a sister of Diane, to speak on behalf of the family.

BRYNA SANGER: I am Bryna Sanger, Diane's sister. On behalf of my family, it gives us great pleasure to collaborate with the SEC Historical Society, especially with Carla Rosati and Richard Nesson, who have been such good partners, in furthering this annual lecture to honor my sister and in some way to continue her work. We are also grateful to Georgetown Law School and to Dean Treanor, who has been gracious to host us today and to lend their distinguished reputation to this event.

This annual lecture is a particularly meaningful way to recognize the importance of Diane's legacy and of her deeply-held commitments. Today is especially significant because of the close connection Diane had working with Professor Goldschmid when he was SEC General Counsel, and with SEC Commissioner Walter, both of whom figured centrally in her life and her work at the Commission. They were her mentors. We are grateful to both of them for helping us to honor her life and her career in this way. Thank you.

RICHARD NESSON: Thank you, Bryna, I am pleased now to welcome William Treanor, Professor of Law and Executive Vice President and Dean to speak on behalf of Georgetown Law Center.

WILLIAM TREANOR: Thanks very much, Mr. Nesson and it's my privilege to be able to welcome you here on behalf of the Law Center. Georgetown has a close connection with the SEC Historical Society since the founding of its virtual museum and archive on the history of financial regulation a decade ago. Professor Langevoort, a member of the

Society's Board of Advisors, hosted a plenary meeting of academics here in the museum's early years that launched this society's Museum Committee. Professor Bob Thompson was also for many years a member of that committee and Don served as a moderator and presenter in some of the museum's past programs and will be part of the upcoming Ponzi Scheme Puzzles broadcast next month. Georgetown has had a close relationship with the SEC and other federal government agencies for millenia.

We are proud that many of our graduates take on public services as Diane Sanger did during her really extraordinary career. Our reputation as an academic leader located in the heart of the nation's capital provides our students with the unique intellectual and geographic convergence of laws and ideas and I am grateful to have the opportunity to welcome you here today. So thank you very much.

RICHARD NESSON: Thank you for your remarks, Dean Treanor. Diane Sanger is a wonderful example of the dedicated individuals, past, present and future who contribute to the creation and administration of fair and effective regulation. At this time, I am honored to welcome another such dedicated individual, the Honorable Elisse Walter, Commissioner of the U.S. Securities and Exchange Commission, and a former colleague of Diane's.

ELISSE WALTER: Thank you so much. I am told that the Honorable although technically yours forever only lasts while you are on the job, so watch out for me later. I am delighted to be here with Diane's family and with the rest of you today at the Diane Sanger Memorial Lecture. Diane was one of my colleagues for many years and a dear and a very loyal friend. Two of those years she worked for me but I think it would be more accurate to say that I worked for her. Diane had rigorous standards and could be a tough critic. My own work often benefited from her insight and I like to think that I occasionally may have lived up to her standards. During frustrating moments at the office, Diane's wit and her wicked sense of humor often salvaged my mood and my sanity. I thought of this side of Diane the other day as I was purchasing the latest piece of décor for my office, a three-foot-wide sign that says "I have flying monkeys and I am not afraid to use them." Now I must remind you that my remarks here this afternoon, including those about the utility of flying monkeys, represent my own views and not those of the Commission, my fellow Commissioners and members of the staff. I can't honestly say how my current colleagues may feel about flying monkeys, although the sign has received rave reviews in its three days in my office. I suspect that if she were here Diane truly would have appreciated my new office ornamentation. On a more serious note, Diane was a zealous advocate for investors and one of the Commission's most dedicated public servants. This passion for investors was matched by another colleague of Diane's in the General Counsel's Office, our speaker this afternoon, the Honorable and he still deserves it, Harvey J. Goldschmid.

When Harvey joined the Commission as its General Counsel in 1998, he was already a distinguished scholar, not just in securities regulation but also anti-trust law which happens to be the second language in my household, so I appreciate that, and corporate governance, another love of mine, having served as a Professor of Law at Columbia and as a reporter for the American Law Institute's Principles on Corporate Governance Project for more than a decade. During his tenure as General Counsel, Harvey helped draft Regulation FD, which promotes fair disclosure to retail and institution of investors alike. He also was an architect of the Commission's adoption of disclosure rules concerning audit committees of public companies. I could go on and on but you want to

hear from him. I understand that the title of Harvey's lecture this afternoon is 'The Future of Investor Protection.' He is particularly well suited to speak about how we address the issues facing investors in the light of the financial crisis and its aftermath.

Harvey's service as a Commissioner began when the Commission was facing the corporate accounting scandals that plagued us all at the beginning of this century. He was critical to the effective implementation of the Sarbanes-Oxley Act which brought important changes to the way issuers, auditors and securities professionals conducted themselves from CEO and CFO certifications to internal controls over financial reporting and reforms to the audit process. These measures have now become fundamental tools for promoting full and accurate disclosure to investors. As Shakespeare wisely said, "What's past is prologue." And these experiences undoubtedly give Harvey a unique insight into the issues facing the Commission today in its mission to protect investors. This is not to say that Harvey's only insights into the future of investor protection come solely from his past service at the Commission. To the contrary, since leaving the Commission in 2005, Harvey remains an active and vital voice in our ongoing mission of investor protection, serving among other things as a Public Governor of the Financial Industry Regulatory Authority, as a Trustee of the IFRS Foundation and as a member of the governing board for the Center for Audit Quality to mention just a few of his positions in leadership. But most important he continues to instruct our next generation of public servants in the legal and securities industry as Dwight Professor of Law at Columbia and on a more personal note, Harvey has been an unfailing source of wisdom for me particularly during my tenure both at FINRA and in my current position where I serve as one of his successors. Please join me in welcoming the perfect choice to deliver a lecture named in Diane's honor and memory, the Honorable Harvey J. Goldschmid.

HARVEY J. GOLDSCHMID: It's always lovely to be introduced by an old friend who's kind and gentle. I must admit that while I really do miss Washington in all kinds of ways, I don't miss the need to give a disclaimer at the beginning of every speech. I am delighted to be here at Georgetown, and I am honored to be giving a lecture in Diane's name. Diane Sanger brought high intelligence, admirable dedication, rigorous standards (as Elisse suggested), and a fundamental commitment to investor protection to all she did at the Commission. Diane's qualities of mind and character illustrated why the SEC -- when at its best -- is an extraordinarily effective institution. In large measure, I associate the survival of investor protection (my title) with the survival and health of the SEC. This afternoon, I am going to discuss contemporary threats to the Commission and then consider threats to two key pieces of modern investor protection legislation, Sarbanes-Oxley and Dodd-Frank.

The years since 2005 have not been easy for the Commission. There was a serious threat of elimination or dismemberment in the spring of 2009, as the Obama Administration began its regulatory reform process. A commentary, for example, in Bloomberg, concluded as follows. "At last we are taking steps to tackle ... the crisis connected to sub-prime mortgages. But when are we going to get around to the fiasco of sub-prime regulators...? Any chance Congress will get smart and dismantle the SEC?" Thanks to the heroic efforts of Mary Schapiro, Elisse Walter and others, the SEC survived in the spring of 2009, and indeed, gained considerable ground in Dodd-Frank (although, as I will discuss later, that has been something of a mixed blessing). But today, I find myself growing increasingly concerned about the naivete and the stridency of current attacks on the Commission. Commissioner Walter, who has spent 30 years as a keen observer and important policymaker at the SEC, said the following recently: "[In

the past three and a half years] we have faced criticism that is unprecedented.” What’s been happening? Basically the Commission has been put under immense and unfortunate pressure by Congress and the federal courts. Congress has been starving the agency at a time when Dodd-Frank and a series of court decisions have added enormously to its responsibilities and workload. Let me briefly reference what I see as the key problems.

The SEC’s budget for fiscal 2012 is about \$1.3 billion, but the budget was frozen from 2005 until 2009 and the SEC lost roughly 10% of its staff and 50% of the budget for new IT systems during that period. Today’s budget, with all the catch up needed in technology and personnel, is not adequate to meet the Commission’s traditional needs. But Mary Schapiro testified that the SEC needs 800 additional staff members, and a doubling of its budget (which was contemplated in Dodd-Frank) in order to meet its new responsibilities for derivatives, hedge funds, rating agencies, and on and on. About two weeks ago, the House Financial Services Committee rejected a proposed \$1.56 billion budget for the Commission for fiscal 2013. I am not very partisan, but the rejection drew the following partisan -- and accurate -- comments: “according to you [Republican members], the SEC wasn’t proficient and according to us [Democratic members] they didn’t have the resources to be proficient. But you don’t make an agency more proficient by starving it.” That’s not a difficult point, but why can’t it have an impact on Capitol Hill.

The Supreme Court and its hostility to private litigation has added large new pressures on the SEC. *Stoneridge* (in 2008) and *Janus* (in 2011) made private litigations under the 1934 Act against lawyers and investment bankers, no matter how intentionally fraudulent their conduct, virtually impossible. Even accountants are largely off the hook. The SEC, with its aiding and abetting authority, now must fill a very large gap with respect to these critical gatekeepers. Of course, the question is again, where are the resources to do that? Remember that the SEC has traditionally said what the Supreme Court repeated in 2007 in the *Tellabs* case: “meritorious private actions to enforced federal antifraud securities laws are an essential supplement, to the SEC.”

In a similar way, the *Morrison* case, in the Supreme Court in 2010, took away from private plaintiffs actions for venal activities in the United States as long as the company was listed elsewhere, or the closing was taking place out of the United States. For the SEC, Dodd-Frank restored the power (under traditional standards of significant conduct or substantial effect) to reach fraudulent conduct that private cases cannot. Dodd-Frank added it back but not for private cases. Which means again a large gap to fill, a large new burden on the Commission. In the lower federal courts, Judge Rakoff’s *Citigroup* decision rejected the SEC’s neither admits nor denies formulation for settlements. Now there is a surface plausibility to what Judge Rakoff did. It is understandable that there would be a distaste for x hundred million dollar settlements, where a defendant does not admit any wrongdoing. Although the fact that the defendant is paying x hundred million, and taking injunctive relief, provides more than a hint of some kind of admission. But in a world where the SEC settles well over 90% of its cases, the elimination of “admit or deny,” the requirement of an admission, would require huge new resources for enforcement; complex cases would take much longer. If Judge Rakoff had the power to double or triple the SEC’s enforcement budget, everything would be fine. But in the real world, the Second Circuit last week indicated it was likely to reverse the *Citigroup* decision and that is the right answer.

Another problem from the lower federal courts comes from the D.C. Circuit. The demanding, impossibly demanding, cost-benefit analysis that was required in the proxy access case, *Business Roundtable* (in 2011), was extraordinarily injudicious and unwise. I think the *Business Roundtable* decision should be offensive to anyone concerned about the proper role of Circuit Courts. The SEC's 60-pages cost-benefit effort was sturdy and deserved judicial deference. Instead it received a hyper technical and unrealistically demanding analysis. Cost-benefit is a legitimate analytical tool. I made no decision while at the Commission without thinking about cost and benefit for those concerned. But the *Business Roundtable* decision barely hid the Circuit panel's opposition to the substance of the Commission's rulemaking. There have been few so blatant comparables in the federal courts since the 1930s. Now, we might live -- but not easily -- with the D.C. Circuit's cost-benefit approach if it had the power and was willing to dramatically increase the budget of the SEC. But I haven't seen either the power or the willingness to do so. Again, the *Business Roundtable* decision is currently putting enormous new burdens on the Commission and other parts of the federal government.

Let me conclude this segment on the following note. Historically, the SEC has had stronger and weaker moments. I would identify stronger moments in the early years with the chairmanships of Joseph Kennedy, James Landis, and Bill Douglas. In the middle years, I would identify the strength of my colleague at Columbia Bill Cary and Manny Cohen. And, with a bias I bring, I think in recent years of Arthur Levitt and Bill Donaldson, both of whom served with great distinction. Indeed, it was just eight years ago, in 2004, at the 70th anniversary of the Commission, that Paul Sarbanes talked about the Commission as the crown jewel of the federal system; that was realistic then and ought to be now. Mary Schapiro and Elisse Walter and others on the Commission have done an excellent job of revitalizing the agency and moving it forward. There have been bumps in the road, of course, but it is a much stronger place then when they came. On the other hand, the years 2005 to 2009 were not the Commission at its best. The Madoff and Stanford scandals, the Bear Stearns and the Lehman failures, and weak enforcement all took a toll. The bottom-line for the period was indefensible passivity. But the message has to be, rebuild, reinvigorate, adequately resource; do not marginalize, starve, or dismantle; otherwise, the survival of investor protection will be very much in doubt.

Moving on to the legislation, I would have thought that serious debate about Sarbanes-Oxley, near its 10th anniversary, would be a non-starter. Sarbanes-Oxley has proven itself time and again. But Mitt Romney earlier this month called for a repeal of Sarbanes-Oxley and the current debate on Capitol Hill on the JOBS Act (before the Senate right now) indicates that I'd better take up the issue. I am going to focus on the current effectiveness of Sarbanes-Oxley on the audit process and disclosure; those are at the heart of Sarbanes-Oxley. But I should emphasize that if I took up other areas I would come to the same conclusion; Sarbanes-Oxley has been a great success.

Let me begin my discussion of Sarbanes-Oxley by bringing you back to the Enron and WorldCom scandals that became public in 2001 and 2002. As Elisse Walter indicated, I joined the SEC at a low moment. I was sworn in on July 31, 2002. U.S. financial markets were then in turmoil and the corporate community was in disrepute. July 30 was the day the President signed Sarbanes-Oxley into law. If helping to restore public confidence had been the only accomplishment of Sarbanes-Oxley, I would praise what was done. The recent financial crisis has again emphasized how critical trust and confidence are to our financial system. But far more than the atmosphere was changed.

Sarbanes-Oxley made dramatic long-term improvements to the nation's audit process and to public company disclosure.

First let me focus on accountants and the accounting profession. I believe that directors, particularly independent directors, are the most significant actors in the U.S. corporate governance system. If all goes well, they provide the checks on senior managers that are critical. But the most important insight to be gained from the scandals of the 1990s and early 2000s, and again from the recent financial crisis, is that even active, demanding independent directors cannot carry the load alone.

The U.S. corporate governance system is heavily dependent on proper disclosure and the effectiveness of various gatekeepers. Accountants are perhaps the most important gatekeepers in the United States. Two key issues faced the Congress and the SEC in terms of Sarbanes-Oxley. First, how to strengthen the relationship between independent accountants and independent directors? Second, how to strengthen the accounting profession itself? On the question on how to strengthen the relationship between independent directors and the independent auditors, the basic corporate governance idea was that independent dispassionate directors would be able to bring a balanced long-term perspective to what was going on. Their dispassionate perspective -- shielded, for example, from the pressures on managers to meet earnings expectations -- would significantly increase the likelihood of avoiding improper earnings management and other overly aggressive or illegal disclosure practices.

A major drive of Sarbanes-Oxley and the SEC (through rulemakings) was to realign loyalties and bring a closer relationship between the outside auditor and the audit committee. Sarbanes-Oxley strengthened the relationship in various ways. It provided a more rigorous definition of independence; it added whistle-blowing provisions; and it permitted the audit committee to retain its own experts.

The most important provision interestingly enough was a very simple one in concept. It said something like, "The audit committee must take direct responsibility for the appointment, the evaluation, the compensation, and where appropriate, the firing of the independent auditor." Now this has had a profound effect. Recently, the CEO of a major public corporation said to me, "Neither the audit committee nor the outside auditor understand that I am the boss." No more. The change has been quite dramatic. Imperfect empirical evidence, my experience in counseling audit committees, work by the Center of Audit Quality, and much anecdotal evidence suggests that Sarbanes-Oxley's audit committee provisions have made a large difference. Today, audit committees are spending more time, putting in far more effort, demanding far more from the independent auditor and corporate managements, and seriously questioning what's going on. The recent financial crisis demonstrates that it's not yet a perfect world, but what is critical to understand is that the evidence indicates without Sarbanes-Oxley, it could have been much worse.

Now I am going to discuss what Sarbanes-Oxley did to strengthen the accounting profession itself and that largely involved the PCAOB. In an amicus brief to the Supreme Court, defending the constitutionality of the PCAOB, which I helped to draft for the Council of Institutional Investors (and other institutional investors), we concluded as follows: "The widespread failure by auditors to detect serious management fraud, which shocked American financial markets, occurred in large part because no one was watching the watchers. The scandals demonstrated the inadequacy of the accounting

industry's self-regulation. "Inadequacy" was about the mildest word we could use. Self-regulation prior to Sarbanes-Oxley involved imperfect rulemaking, very little in the way of discipline, and inadequate inspections of audit quality. The PCAOB greatly enhanced all of those and wisely put much of its budget into inspections. Also, Sarbanes-Oxley eliminated the excessive consulting that resulted in enormous pressure on auditors. Anyone who tells you Sarbanes-Oxley hasn't had a profound and affect in the US system is simply blind. Of course, the constitutionality of the PCAOB was basically upheld despite relatively trivial modifications of the PCAOB's status.

Let me turn to the most controversial part of Sarbanes-Oxley and that was Section 404, the internal controls provisions. The 404 provisions are correctly described as the one, but I emphasize the word one, large dollar cost item in Sarbanes-Oxley. All of the other claims of excessive Sarbanes-Oxley cost are largely fanciful. But in terms of 404, as the first Chairman (Bill McDonough) of the PCAOB kept saying, "How can you have a strong reporting and disclosure system -- or corporation -- without strong internal controls? Won't the expense be worth it?" The answer from me is emphatically "yes". Now 404 was implemented, and let me be blunt, quite imperfectly. There is more than enough blame to go around; the SEC, the PCAOB, the accounting firms, and public corporations all had missteps and wasted efforts. But relatively quickly, in terms of the rulemaking process, the SEC and PCAOB made corrections with the help of the profession. The rulemakings took account of the need for risk assessment, for use of judgment, and for reliance on prior work. And today 404 represents a cost-effective and wise public policy prescription. Yet it's now being challenged on Capitol Hill; for the smallest companies it's already gone. For public corporations with up to a billion dollars of revenues, or \$700 million of market float, its continued application during the first five years of an IPO is very much in doubt. Mary Schapiro concluded last week that the "current version" of the so-called JOBS Act "goes too far in diluting investor protection". More bluntly, Arthur Levitt called the legislation "the most investor unfriendly that I have seen in 25 years".

I associate myself with both of these critiques. Investor trust in the fairness and integrity of our financial markets gives the U.S. a great comparative advantage in terms of capital formation and jobs. This is what we must hold. It is extraordinarily unwise to jeopardize the trust of the public (50% of whom invest) with the kind of deeply flawed legislation that they have been debating on the Capitol Hill this day.

I only have time to briefly discuss the disclosure provisions in Sarbanes-Oxley. But let me just emphasize the certifications, the additional disclosure required, the more timely disclosure, all of those have created a disclosure system that's in much better shape than once was the case. There was a payback. In my last public meeting as a Commissioner, in 2005, we deregulated a fair amount of the 1933 Act. We made the 1933 Act process more effective, more efficient, and less clumsy, without the loss of investor protection. There is nothing wrong with deregulation, if you understand what you are doing and why. I hope and pray that in ten years we are going to be able to say something along these lines about the JOBS Act.

I will take just a minute, or two on Dodd-Frank. Let me give you my overall evaluation of Dodd-Frank. It's put the United States in a much better place than we were before it was enacted, but it certainly is imperfect legislation. It could have been drafted to produce a stronger and more effective regulatory scheme and to avoid at least some of the uncertainty that it has created. I want to make three basic points about Dodd-Frank. One, it's new legislation, enacted in July 2010. The 2,300 pages of Dodd-Frank

establish a framework. An immense amount of new regulatory authority has been granted to federal agencies, but often with only limited Congressional guidance. We are quite dependent on the agencies using their authority wisely. Most key implementing rulemakings are still works in progress. In many ways, it's too early to seriously evaluate Dodd-Frank. I suspect there will be bumps in the road for Dodd-Frank much as 404 was a bump in the road for Sarbanes-Oxley. But in the end, if you go to a year like 2022, I believe that Dodd-Frank will be judged a success. Second, the "get government off my back" attacks on Dodd-Frank and Sarbanes-Oxley ignore the costs of Enron, WorldCom and other turn of the 21st century scandals. More importantly, they ignore the indefensible greed, tolerance of excessive risk taking and leveraging, and breakdowns in institutional responsibility (e.g., by mortgage banks, Wall St. broker-dealers, and credit rating agencies), in the private sector, which were a primary cause of the financial crisis. In terms of government regulation, there were clearly serious failures by the Federal Reserve, other bank regulators, and the SEC. But the government failures largely involved "sins" related to passivity and excessive trust in markets. Dodd-Frank should help to discourage our going back to a madly passive, deregulatory world.

Third, Sarbanes-Oxley significantly enhanced the enforcement power of the SEC. Dodd-Frank greatly added to SEC's regulatory responsibilities. Sarbanes-Oxley made available to the SEC new civil penalty and disgorgement powers, easier to obtain officer and director bars, broad equitable remedial powers, and for the Department of Justice, enhanced criminal sanctions for venal and willful conduct. When the SEC is properly active, these enforcement powers help to create the requisite deterrence and accountability.

If our securities regulatory system is to work, senior corporate executives, Wall St. types, and various "gatekeepers" must know that they are likely to be held accountable when wrongdoing occurs. Effective deterrence requires a strong, credible threat. It is that "threat" that creates powerful incentives to avoid wrongful acts and to bring about the cultural, procedural, and process changes necessary to protect investors.

Sarbanes-Oxley enhanced accountability and deterrence. Dodd-Frank has a similar potential, but the current political atmosphere and the deadlocks on Capitol Hill leave me concerned about the future. As with much of Dodd-Frank, it is too early to be certain where we are heading.

Basically, at issue today is whether we have the will and wisdom to maintain and strengthen investor protection, or whether deregulatory slogans and ignorance will cause us to lose our way. For me, long-term investor trust and confidence are the keys to making our financial system work.

As the SEC Historical Society might remind us, it would be nice if those power, in this great city, learned the lessons of the past.

RICHARD NESSON: As Mr. Goldschmid has indicated he will take questions from people here in the audience at Georgetown. So if you have a question please step to the microphone in the center and speak up so that people here as well as online can hear you. Thank you.

HARVEY J. GOLDSCHMID: Here comes someone. Looks like a student, I am worried.

CHARLES LEE: My name is Charles Lee. I am an LLM candidate at the Law Center. And I was wondering if you could share with us what aspects of the House's version of the JOBS Act you think are good ideas in that they further capital formation without hurting investor protection.

HARVEY J. GOLDSCHMID: The concept of an "entry ramp" is worth considering. Whether every small public company needs the panoply of investor protections we think appropriate for GE is a legitimate question. But remember just about every empirical study shows that fraud is more likely to occur in the small public corporation than in the large. The economic consequences of an Enron or WorldCom failure, however, are, of course, dramatically larger. The entry ramp the House version constructs is much too wide and long -- companies can have up to \$1 billion of revenues and \$700 million of market float and still be on the ramp. Section 404, the corporate governance provisions in Sarbanes-Oxley, and other investor protection provisions should be applicable to any corporation anywhere near that size. The so-called "crowd funding" provisions of the House version, with realistically no investor protections, are an invitation for fraudsters and the greedy to fleece working families and the aging. As is obvious, the JOBS Act is not my favorite piece of legislation.

DONALD LANGEVOORT: I want to take you back to what you were talking about with respect to the auditing standards that underlay 404. You described the first step as a missed step that got corrected a few years later with auditing standard number five. Obviously a lot of damage was done by the missed step politically setting in motion a campaign in corporate America to get rid of this. Why did the missed step occur?

HARVEY J. GOLDSCHMID: Well, let me give you a little of the history. I sat with the accounting profession and said, "Are you ready to go? Do you understand the internal controls standards well enough and the guidance well enough?" And the answer was always yes; never we need more time. But both the accounting profession and issuers needed more time and there were people working on internal controls who didn't have a clue. An issuer reported: "the accountants came in and went to the warehouse; they counted five cameras in the warehouse and they said we need a sixth". What had the sixth camera to do with internal controls for financial reporting? The SEC and particularly the PCAOB rulemakings were imperfect, although Alan Beller, who led the SEC effort, is first rate. But it wasn't clear enough that you could take account of risk, you could use judgment, and you could rely on prior work done. There is no doubt there were mistakes. But did we correct relatively quickly? Yes but it hurt the SEC and 404.

But what is around today is a kind of urban myth. Section 404 is not excessively expensive any more, and the payback is much greater. Section 404 should not seriously inhibit IPOs, and we ought to keep in mind, not every company ought to be public, or ought to have the money of public investors. We have too many people who are not going to understand this new ramp Congress is creating. You can make a case for a ramp, and Don, you have done that. But not the ramp that is in the JOBS Act. And you don't want people saying, "We will not invest. We cannot trust this process." If you care about jobs, losing that willingness of Americans to invest, in the long term, is highly destructive.

MATTHEW BIZONTZ: Hi. Matt Bizontz, JD candidate. Touching on your earlier comment about the self regulatory aspect of the accounting profession, I was interested in your comments on some of the proposals to deal with self regulation of the broker-

dealers through something like FINRA and the sort of effectiveness of a FINRA-type entity to deal with that new issue of Dodd-Frank.

HARVEY J. GOLDSCHMID: FINRA is quite different than the AICPA's self regulation of the accounting profession that I described. The old AICPA system was a largely in-house operation with virtually no outside oversight. The disciplinary process, which was run by a very decent group of people, was structured in a way that prevented real enforcement. The standard settings were done with protective instincts in terms of accountants. And, again, the peer reviews were imperfect to say the least. The new, effective model that Sarbanes-Oxley established is represented by the PCAOB, which is appointed by the SEC, with a budget that gets approved by the Commission, and with an independence and vigor not found in SROs. Moreover, the SEC must approve just about anything of significance done by the PCAOB and its monitoring is relatively intense. I believe that the PCAOB model is now working very well.

I bring a certain bias to any FINRA discussion: as Elisse indicated, I have been on the Board of Governors of FINRA for some years. It's a very decent and able group. It does a good job. The question is how much do you gain or lose by having a heavy industry representation? The board is made up of about 22, and I think there's a majority of one in terms of independent directors. The advantage is you do get serious industry input, and you do get serious concerns about efficiency, effectiveness, and cost. The emphasis on efficiency might otherwise be lost in terms of how the broker-dealer world works. On the other hand, there is at times arguably a bit too much industry input. I am satisfied FINRA works. Indeed, I think that when it comes to investment advisers, who realistically have too little oversight, it would be much better to have FINRA responsible or some group like FINRA.

In summary, the AICPA model just doesn't work. FINRA works fine but with a need for balancing. The PCAOB model has been effective, and in general, seems to be running very well.

RICHARD NESSON: Professor, thank you from all of us here as well as the audience online for sharing your wisdom and your experience. For the benefit of those who are unable to attend today's lecture it is now permanently preserved in the virtual museum and archive at www.sechistorical.org. We hope that today's program recognizes all those currently working in the regulation of financial markets, and that Diane Sanger's life serves as an inspiration for those considering such a career in the future. Good afternoon.

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