Securities and Exchange Commission Historical Society
Interview with Alan Rosenblat
Conducted on June 12, 2007, by Kenneth Durr

KD: This is an interview with Alan Rosenblat on June 12th, 2007, in Washington, D.C. by Kenneth Durr. I want to take you back to Chicago. Looks like you went to school there. Were you a native?

AR: No, actually I was not. I went to the University of Chicago College. That was in the Hutchins days.

KD: Robert Hutchins.

AR: You remember Hutchins. And that was in the waning years of the Hutchins' days; and after I went to the college, and then law school. How I got to Chicago is very interesting. When I went to high school, I studied photography. I didn't take any math or languages. And so when I ended up in New York ultimately—because we were living in Buffalo, but I was in the Navy for a couple years—and when we ended up back in New York, I thought I would go to night school and get some credits in languages and math. And of course I never got around to that. I was working in a photo studio. And then one of my best friends from my boyhood in Buffalo came to New York, and he said, "What are you doing in this dark room?" I told him that I would like to go to college, but I didn't have the credits. And he said, "I'm at the University of Chicago. There are no academic requirements except a high school diploma. And you can take an entrance exam. You can take it here. And if they accept you, you go to Chicago." And Chicago then had a very interesting system, which was they did placement examinations. When you first got there they gave you a series of examinations in the arts, and in the humanities—including music and literature. And I did pretty well on those things, because I was twenty-three years old, and I had always been a rather bookish person, and read a lot, and was very interested in art, and studied music, color theory and paintings. And so I did pretty well.

So as a result of that I had only to go to college for two years and a quarter—they were on a quarterly system then—to get my bachelor's degree. Which was fine. And I did extremely well. I graduated with general honors, which meant that I had all A's and B's, and more A's than B's. Unfortunately, however, that meant that my years at the University of

Chicago College were not enough to satisfy the Phi Beta Kappa requirements. So I didn't make Phi Beta Kappa, although some of my law school classmates did. Anyway, I went to the law school. I did pretty well. I got on the *Law Review* and became managing member. There was a professor named Bernard Meltzer who died very recently. I never took a course from him, but if you were on the *Law Review,* he would help you. He knew somebody in New York, and he found this law firm in New York. In the meantime, I had already gotten a job. My tax professor actually got me a job in Chicago. And I was all set to do that. It was winter, in between quarters; I was in Chicago in the dorm, and I said: Why are you in Chicago? And the answer was: Because your mother is in New York. So I said: Is that a good reason? And the answer was no. So I packed up and went to New York. And in the worst time of the year—although I had gotten some introductions from the Dean of the Law School, who was Edward Levi, who later became Attorney General in the Reagan administration. And so he gave me some letters of introduction to some judges in the D.C. courts, but apparently, I didn't excite any interest there. And so I was stranded in New York, living with my mother, and studying for the New York Bar. And so ultimately I got this job. I was really very naïve in the ways of the world, because I didn't tell the tax law professor that I had done this. And he found out that I had left town without taking this job, without telling him. He was really very angry at me. But luckily, Bernard Meltzer put me in touch with a New York law firm.

KD: What was that law firm you got the job—?

AR: The name of the law firm was Hellerstein and Rosier. It was a small law firm. It had two partners, and then they made one of the associates a partner. They did corporate taxes. And I liked that, because when I took the tax course at the law school, I was so frightened that I studied more for that than anything else.

KD: Did you have any sense that you might specialize in corporate and securities law?

AR: No. None whatsoever. They specialized in the consolidated financial statements. And their main client was a large public utility holding company that actually owned the company that owned the Three Mile Island reactor—although that was way before the leak incident. And so I worked there, and I liked it very much. And I liked doing tax work because it's a discrete body of law, and you don't have to worry about some obscure state law decision that you have overlooked. A friend of mine named Marvin Chirelstein, who was a year ahead of me at the University of Chicago Law School, was at Willkie Farr. He was knowledgeable about federal tax law because he had worked for the American Law Institute tax project. Somebody in Chicago who wanted him to come out there, and do tax work in-house at this corporation. And Marvin didn't want to go to Chicago, because his mother was in Chicago.

KD: We've heard that one before.

AR: She had a seat on the Chicago options exchange. And so he put me onto this fellow, his name is Derald Ruttenberg, who had this small company. It was owned by Ruttenberg and two other guys. One of them was an accountant, although a very flamboyant accountant. He owned two Stradivariuses, a violin and a viola, I think; and he played the violin himself, and he liked to do string quartets. And then this other guy named Keith Kindred had a municipal bond house. I used to go to lunch with some of the guys that worked for him, and one of them said, "Don't tell my mother I work in a bond house. She thinks I work in a whore house." So anyway, he financed their ventures, which were directed to buying up distressed companies, taking control of them, and then liquidating the assets. And one that they did when I was first with them was a company, which owned a brewery and some valuable real estate in Chicago. And they also built their own trucks. The name of their truck company was the Available Truck Company. And so they liquidated that, and made a lot of money selling the real estate. I found out that I had come out to Chicago to replace someone who was working there who was very bright. Ruttenberg was dissatisfied with him. And it turned out that Derald Ruttenberg was looking for another Derald Ruttenberg, and there wasn't any; and if he ever found one, he probably wouldn't be able to get along with that person.

So after maybe a few months, he discovered that I was a pedant, and I did good, boring research, but I was not imaginative—I was not a deal-maker—which was the furthest thing from my mind. So I ended up working for the guy that I came out to replace. Which was okay. And it was very good because I learned how businessmen think, from that experience. For example, they took over an iron foundry in Wisconsin. One of the legal questions I was asked to research was: We're taking over this iron foundry, and they use a lot of sand, and a lot of the workers develop silicosis through the years of working with the sand. Would it be legal if we fired everybody who had been there for a long time, to avoid liability for silicosis? And I guess—unfortunately, the answer—at least the answer at that time was no, it wasn't illegal. So that was one little insight I got into—into the way these particular businessmen thought. They were honest. The fact that they asked me to research it showed that they were honest. I did a lot of very routine corporate work, filing state tax returns, and the like. And then the three of them decided to split up, and so they didn't really need two people full-time on their legal staff. They didn't ask me to leave, but it looked like my job was not long to go.

By that time, my friend Marvin Chirelstein, who got me out to Chicago in the first place, was working at this large Park Avenue law firm, Kaye, Scholer. It was Kaye, Scholer, Fierman, Hayes and Handler. I don't know what they call themselves now. So I had tried to get a job with them before, but had not gotten in. But they were expanding rapidly, and they got me in on a weekend and interviewed me, and offered me a job on the spot. And I didn't realize that the person I was talking to was Mr. Hayes, of Kaye, Scholer, Fierman, Hayes and Handler, and not the hiring partner. And the hiring partner was annoyed that they had hired me without his knowing it and without his presence. Which didn't bode well for my relationship with him. In any event, I did some very interesting work at Kaye, Scholer—ordinary corporate work and some SEC work. And I was there for maybe four and a half years, and it didn't look like it was going anywhere. So I decided that I really had to get out. And I had had a friend at Kaye Scholer who had worked at the SEC. And he said, "The place for you is the SEC."

KD: Who was that?

AR: It was Nicholas Wolfson. He said, "Go to the SEC." And so I interviewed in the New York Regional Office. They offered me a job because of my academic record, and the fact that by this time, I had almost ten years of experience as a lawyer. Wolfson said, "The New York Regional Office is okay, but their pay grades are limited, and not as good as in Washington. So go to Washington." So I arranged for an interview in Washington. And at that time, you had to take an examination that had a securities law problem that had to do with a charitable organization, and whether it would be recognized as a charitable organization by the SEC. In the morning, you wrote the exam, and then after lunch you came back, and a small group of SEC staff members interviewed you. They looked at my exam, and they said, "You did very well on this. We are going to send you around to interview some other people at the Commission." So they sent me to the Office of Opinion

Writing, what was then known as the Division of Corporate Regulation—later became Investment Management.

I first interviewed at the Opinions Office, and they wanted writing samples. And I felt that that was somewhat demeaning, after I had had ten years of experience. So I just waited for the next interview. And I interviewed in the division of Corporate Regulation. And there I found someone who was to be my mentor.

KD: Who was?

AR: His name was Solomon Freedman. I think we took an instant liking to each other. And he offered me a job, and I took it. Now I took a pay cut. I was making about thirteen thousand dollars at Kaye, Scholer, and I went down to a little more than eleven. But it was enough to live on. So we moved to Washington—my wife and my first child—my son. And then I worked in the division, reviewing applications for exemption from various provisions of the '40 Act—learned about the '40 Act. And then there was an opening in the Chief Counsel's office, and I don't know whether I applied for it or they asked me—I think they asked me. And I ended up working in the Chief Counsel's office, which was really a great place to be. At that time, the Chief Counsel's office did rule proposals and considered comments on rule proposals, and did the final rule, rule release, and also no-action letters, and interpretations.

KD: How long were you in the Investment Management Division?

AR: I was there from 1964 to 1976.

KD: So when you went into the Chief Counsel's office, this was in the Division of—

AR: Division of Corporate Regulation.

KD: Right. Which dealt with investment companies.

AR: Right, right. And later the Investment Advisers Act. And—

KD: But not at that point though?

AR: No. No, that was later. That was when Casey came in and reorganized the whole thing. I will tell you a little story later about that shocking event. In any event, the Assistant Chief Counsel left, and I became Assistant Chief Counsel. And then there was an opening for the Chief Counsel—his name was Frank Kelly and he went out to California to be in-house counsel with somebody. And so he left, and there was a vacancy. And then, at one point—one of the nicest things that ever happened to me in my life was I was called into Sol Freedman's office, and he said, "We now have a new Chief Counsel." And that was really great. And that was, I think maybe in some ways it was the best job I ever had at the Commission. But there it was, and I had three or four people working for me who were really bright. One of them was Marty Lybecker, and he was really great. Irving Pollack used to say, "If you want to do well, hire people who are smarter than you are." And that was Marty. Marty Lybecker, with whom I still keep in touch, knows everything and remembers everything. And he remembers things that I did that I have forgotten.

KD: Remembering is the trick.

AR: Right. So then I was there. And then one day I was called up to the Chairman's office. Roderick Hills was then the Chairman.

KD: Yes, we're moving ahead a bit.

AR: He called me up to his office. That's the first time I ever sat in the Chairman's office talking to the Chairman alone. And he said, "There's something that I would like you to do. I would like you to go to the General Counsel's Office for a while—you know you don't have to go if you don't want to—just for a little while, and then you can go back to where you want to go." And that was a shock because I knew very little of the General Counsel's Office, although I knew they were all very good. And I asked around, and everybody that I asked said, "The General Counsel's Office is the place to be. You ought to go there." So I went there. And then Harvey Pitt, who was then the General Counsel—he wanted to have people from the Divisions working for him, so he would know what the law was, and what the pros and cons were of the things that the Divisions were proposing and doing. He got one other person to come up, and I guess the guy from Market Regulation—it was then known as Division of Trading and Markets—refused to go. I didn't know you could refuse, but he did. Harvey was a very hard taskmaster—very, very hard; very critical—very hard to work for. And I did something that I never wanted to do, which was appellate litigation. Now I had done some appellate litigation at Hellerstein, when I first got out of law school; and I wrote a brief in a case that we actually won about a million and a half dollars in this case from the government.

KD: Why didn't you want to do it?

AR: I didn't want to do it because the deadlines are real. And you have to write briefs. And then depending on the difficulty of the brief and who was reviewing it—and it was often Harvey—and how long it would take to get it reviewed, and what would happen if you got it reviewed. Harvey, at least on one occasion—I had worked on this brief and given it to him several days before the brief was due. He saw me the day before it was due and he didn't have any substantive criticisms, but the only real thing he wanted me to do was put the first part at the end, and the last part at the beginning. Now we had no word processors. We used to do cut and paste. And it was really very difficult. Of course I did it, and it was fine. And so that's one of the reasons why I didn't like appellate litigation. I actually did two or three oral arguments. I hated that too, because it's very nerve-wracking. But when you get up there, there is nothing like it. I went to an oral argument in San Francisco, and the question was: Can a corporation assert the right against self-incrimination? And the clear answer was no. The morning of the argument, I arrived at the courthouse early, and found out who the judges were. And one of the judges was Justice Clark, who had been on the Supreme Court, was then doing the circuits. And he was sitting on this Court of Appeals in San Francisco. I quickly did some research in the cases. I looked at some of the cases that I had had in my brief, and I discovered that he was Attorney General and wrote a brief in a case that I had cited. So when I got up to argue that there is no right against self-incrimination by corporations—I said, "Well in the X, Y, Z case, which Justice Clark won, when he was Attorney General, the court held that there isn't any right against self-incrimination by corporations." And later on, when one of the other judges questioned me, Justice Clark interrupted and said, "Oh, that was decided in the X, Y, Z case that I won." So we won that case. So yes, there's nothing like doing it, but working up to it can be torture.

Well then, ultimately, they got somebody in the Office of the General Counsel who had been doing legal aid work. He knew how to organize lawyers' work. He didn't know anything about securities laws, but he knew law office organization. And he recommended that they break the office down into appellate litigation, and counseling, which involved reviewing memos that the Divisions sent to the Commission, either for enforcement or for rule-making. And he had interviewed me, and he knew that that's what I wanted to do. So just before Harvey left, and Ralph Ferrara became General Counsel, and I worked for Ralph. And that's when I really started enjoying it, because, if any question involving the Investment Company Act arose I could advise Ralph what position to take. And same thing on legislation, amendments.

I left out one extremely important thing. When I was in the Chief Counsel's office in the Division, the Commission recommended what became the 1970 amendments to the '40 Act. I did a fair amount of work on it. Dick Phillips in the General Counsel's Office and others worked on it, but I did something toward the end—went to the hearings, reviewed and wrote of testimony. And that was really a lot of fun because ultimately the 1970 amendment passed. Although if you read the book—I forget—it's a book by somebody who took over on Loss's securities law treatise—

KD: Yes. Seligman.

AR: Seligman. If you look in Seligman's book, you see that he said that the '70 Amendments didn't do anything. It was a failure. That is totally wrong. As many Investment Company Act lawyers will tell you, it made the whole thing different.

KD: Well I want to talk about that. I want to approach that from the other end.

AR: Yes, okay.

KD: And I want to jump back a little bit. We've got you into the SEC, and through to Assistant General Counsel. Jumping back: even before you came, I was intrigued to see during your Kaye, Scholer time you were involved with a case called Cady, Roberts.

AR: Oh yes. Thank you for mentioning that.

KD: Now did you know you were in a landmark case here?

AR: Thank you. Yes, as a matter of fact, the first few words in that case were, "This is a landmark decision." That was Chairman Cary. That was Cary who did that. Yes. Thank you for reminding me. I remember I was in my office at Kaye, Scholer, and somebody came into my office and he said to me, "What would you think if somebody had some information that was very valuable about a company, and you're a broker/dealer, and some of your clients had stock in this company, and you had discretion to sell their shares in this company, and you knew that the stock—as soon as this information became available, the stock would go way down. And you did that. Would that be illegal?" And I said, "Absolutely not, because there's no face-to-face dealing. Someone who doesn't know the other side, and trades on an exchange, has no duty to the other side of the trade, if he trades on based on the information."

So now, this was very interesting because the New York Regional Office had brought this case. It was an administrative proceeding. And the parties, except for Robert Gintel, the man who used the information, settled the case, in terms of liability. The only thing that involved in the settlement for our client Cady, Roberts was the penalty. Now Robert Gintel later went into the mutual fund business. But anyway, he did not settle so his part of the case was arguing that it wasn't illegal. And the General Counsel of the Commission, Philip Loomis—who later became a Commissioner—argued for the Commission. I forget who argued for Cady, Roberts, but in our brief, we said, this is unprecedented. We found no case in which there were not face-to-face dealings, and so it couldn't possibly be illegal. And as you know, the Commission held otherwise.

Now I will tell you something about the Cady, Roberts case. I've mentioned this before in public. Cady, Roberts, a brokerage firm, had a large amount of Curtiss-Wright shares in clients' discretionary accounts, and a representative on the board of Curtiss-Wright, Robert Gintel. Curtiss-Wright had been doing badly, but it had not cut its dividend. It was paying dividends out of past earnings. And the question at this directors' meeting was: Shall we cut the dividend? And so they decided to cut the dividend. Now the New York Stock Exchange rules at the time required that you send a telegram to the New York Stock Exchange to appear on what they called the broad tape, the Dow Jones news service tape, saying that you'd cut the dividend. And so then, after they decided to cut the dividend, they had a short restroom break during which time, the secretary of the Chairman of the Board of Curtiss-Wright went to type out the telegram. But she was not in her office. They were having this meeting in someone else's office. And none of the secretaries would let her use their typewriters. And so finally she found one, and she typed out the telegram, and they sent it. But by that time, Gintel had called his office and got someone to tell the trader at his firm that the Curtiss-Wright board had cut the dividend, and the trader immediately sold all the Curtiss-Wright shares in Cady, Roberts clients' accounts. Now it is quite possible that if she had been able to find a typewriter earlier, the news would have been public, and the Cady, Roberts case never would have happened.

Another interesting wrinkle was that there was a New York Stock Exchange rule that if you sold short, you had to label it short. But they didn't label it short because they were selling it what they call 'against the box,' because they owned the shares. They actually had the shares in discretionary accounts. So it was a sale 'against the box.' And so one of the things that happened was they didn't mark it short. The New York Regional Office was investigating this sudden suspicious drop in the shares of Curtiss-Wright, and they finally found our client. But it's interesting that they knew that there wasn't any law on their side, and they had to go to the Commission. And Chairman Cary came through for them.

KD: Yes, and the rest is history.

AR: Yes. Actually, I think one of the reasons why I got hired at the SEC was I told them that I had worked on that case. And I still remember being in a seminar with Loomis that he held on interesting issues. And the question he raised was: "Suppose the information you had was not really information about the company—the working business of the company, but just market information; information, for example, that one of their directors or officer was going to sell out his shares. Would that violate Rule 10b-5?" And Loomis said, "No." But the Commission ultimately said: "Yes."

KD: It took them a while to do it.

AR: So that shows how the law develops in very unexpected ways.

KD: Right. Well let's go into the Division of Investment Management. You talked a little bit about coming in at the beginning, and learning about the 1940 Act, the Investment Company Act and the Advisers Act. My sense is: because you've got that completely different set of legislation from the '33 and '34 Acts, that there's something different about that division—the kind of work, and maybe even the kind of culture. Did you find that?

AR: Oh yes. Well as you know, as I said before, we didn't have the Advisers Act until Casey reorganized the division. And that was a shock because I went home on a Friday, and when I came in the following Monday, my office was gone, and all that there was the iron supports for the plasterboard. And I didn't have a phone connection to or could see my secretary, so I went out and bought two toy walkie-talkies. And I used to call her on the walkie-talkie. And that was interesting. We got the Advisers Act, and that's when I started to learn about the Advisers Act, which was a whole new thing.

KD: Okay. But when you first went, you had the Investment Company Act?

AR: Right. Yes. Right. And I didn't have the '34 Act, very little of the '33 Act. Although I had done a few filings at Kaye, Scholer, '33 Act filings. You know I still don't consider myself an expert on the '34 Act. I'm a little bit more comfortable with the '33 Act. But since what I currently do doesn't involve the '33 Act very much directly.

KD: The 1940 Act is another matter.

AR: That's it. Right. Yes.

KD: Now, when you came in, it had only been a short time since there'd been a study done by the Wharton School.

AR: Right. Yes, that's right.

KD: Was that influential? Did you hear about it? And did you study the findings?

AR: No, I think Phillips and some of the other people—well, there was the Wharton School Study, and then there was a Special Study. And so the Special Study came after the Wharton Study, right?

KD: Correct. Yes.

AR: And there were still some people at the SEC who had worked on the Special Study.

KD: That would have just wrapped up about the time you came in.

AR: Right. Right. The '70 Amendments built on the Special Study, but was a whole different kind of exercise. We went through two full sets of hearings. And as a matter of fact, it almost went down the drain. Hamer Budge, who was a conservative Republican, who knew Richard Nixon when they were both in the House of Representatives together—that's how he became Chairman. He was in Nixon's Chowder and Marching Club. And he had actually been persuaded that the '70 Amendments—what became the '70 Amendments—were worthwhile. And when he heard that no one was pushing it, even though we had two full sets of hearings, he became very upset. And one of the Commissioners who came from Congress, I think, was a representative—I can't remember his name—Budge sent this guy over, and he used to walk the halls, and buttonhole people, or go into their offices, and try to persuade them to push the '70 Amendments. And that's how it happened, because Hamer Budge was very upset, and really believed in it, and was told: It's not going anywhere. No one's interested in it. There's too much to it, it's too hard to understand. And that's how it happened.

And one of the interesting things that happened in the '70 Amendments was this question of Section 36(b), which imposes a fiduciary duty on investment advisers for the amount they receive in compensation. We could not get the fiduciary duty in an amendment to Section 15 approved. And during one of the hearings—I think it was Senator McIntyre from New Hampshire, there was somebody from the ICI testifying, Robert Augenblick. He was the president of the ICI. Senator McIntyre said to him, "Now you're against putting a fiduciary duty into this statute. Wouldn't you agree that there is a fiduciary duty on the part of an investment adviser?" And so he said, "Yes, there is." So instead of amending Section 15 to make it provide that fees had to be reasonable, they put it in as an amendment to Section 36. That's how we got Section 36(b), which says that an adviser has a fiduciary duty.

KD: Is this related to 22(d)?

AR: No. Has a fiduciary duty with respect to the amount of compensation.

KD: There was a lot of gray area, as far as how do you determine what is reasonable.

AR: Yes. We thought that that was a great coup, getting that in 36(b). But the courts went—and Dechert's clients are happy about this, and other law firms—the courts went in an entirely different direction from what we had predicted. And very few cases were litigated because people settled. They settled by lowering the fee and putting in break points, for a number of years, and then paying cash. I think there were only a few litigated cases, and in the litigated cases, I guess Gartenberg was the one that is the most cited precedent. Instead of focusing on what the adviser did, and what was reasonable with respect to duty—and I'll add something to that—they focused on what the directors did, what they considered, what they looked at, whether they were diligent in analyzing the information they had gotten. If the directors said: Well everybody's getting a half of one percent with no break points, that's what we're going to do. For all practical purposes, that was okay. Now another word about reasonableness: when they were doing their formal statements, introducing, and supporting the '70 Amendments, one of the senators—I think his son is a Senator now too, from Utah—Senator Robertson of Utah, I think—got up and he said, "These amendments provide a standard of reasonableness for advisory fees." He couldn't have said it better for the Commission, although it didn't do any good because, as I said, the courts went in an entirely different direction. Wearing my old SEC hat—I've always liked to believe that Section 36(b) put a cap on greediness on the part of investment advisers, and made them be more circumspect in what they were doing. And it did a lot of good.

Now one of the interesting things is, is in my later work at the Commission, I was on the Task Group of financial regulatory agencies, including the Federal Reserve Board, the Comptroller of the Currency and the CFTC. I was the SEC representative. The ICI argued to the Task Group that all 36(b) does is cost money because you have to hire lawyers, and the litigation is very, very expensive. And on a cost-benefit basis, 36(b) is not worth it because it costs shareholders in legal fees more than it's worth. When I heard that at this meeting of the Task Group, I went back to my office, and I did some research on the settlements. And I added up very quickly the dollars that funds had gotten in these settlements. And it was a very surprisingly large amount, not even counting the reduction in the advisory fees, but just the cash settlements. And so at the next meeting of the Task Group, I brought that up. And I said, "Look, this shows—" I also told Chairman Shad that the figures just go the other way on a cost-benefit analysis. And so he didn't object to my taking that position on behalf of the Commission at these meetings.

Richard Breeden was representing the Vice-President, who was Bush, Sr., on the Task Group. And he was the Chair. He was a very effective Chair. He would not let things go on and on. We wrote a report, which is a fairly good report. It has some stuff in there about the '40 Act that really was not too bad, and about the investment advisers. There's something in it that says that the Commission takes the position that giving any advice about securities, even though it's not limited to specific securities, requires registration under the Advisers Act. And so there's something in this Task Group report that says that ought to be changed.

KD: If you're not giving advice about specific securities, then you don't have to be registered?

AR: No, no. The position of the Commission then was—and I don't think it is anymore—if you advise somebody for compensation other than brokerage fees—if you have a client—if you're a broker/dealer, or you have a client, and you say: Here's what I think you need to do with your asset allocation. I think you need—your resources are twenty thousand dollars a month—I think you ought to put ten thousand dollars into life insurance, five thousand—X dollars into real estate, and X dollars in securities—the position of the staff was then that if you did that, you had to register under the Advisers Act. And then the Commission—yes, now it's all coming back to me, like a bad dream—and then the Commission brought a case, which I helped write the brief on, and lost. And the name of the case….

KD: Lowe.

AR: The Lowe case. In the Lowe case—this is a guy who did newsletters—yes, this is all coming back. Lowe sent out newsletters, and he may have made a specific recommendation about securities, but he didn't tailor his advice to the specific needs of any client or customer. He had been kicked out of the advisers business by the Commission—this was really a bad guy—this was a guy who stole some money from a customer, and then tried to settle with the customer. And he brought a copy into the court of a photocopy of a check that had ten thousand dollars on it, except that he had altered the check. It was really for a thousand dollars. And so the judge in that case didn't take too kindly to that either. This was the kind of guy we were dealing with. In the Lowe case, the Second Circuit said: In order to be required to register as an adviser, an entity must give personalized advice. It has to be directed to the specific financial and other needs of the client. Now the funny thing about that was, Lowe didn't make that argument. He just made a generalized unconstitutional argument, and it was some association of journalists and writers who had written an amicus brief who took that position. And when I read that brief I laughed. And I said, "This guy must have dictated this into a dictating machine at two o'clock in the morning before he fell asleep." But that was the thing that won the day. That won the day.

KD: Well it was this idea that he was speaking in general terms through his newsletter, he wasn't endorsing something to someone specific?

AR: No, as a matter of fact, he may well have made—no, I'm sorry, go back—he probably did make specific recommendations, but those recommendations were not specifically tailored to the needs of anybody. You could read the thing, and you could take it or leave it. And there was no discretion involved, which is very important. And for example, when *Money Market* magazine first came out, the question was—and they had a lot of specific recommendations—it's a *Time* publication, I don't know whether it's still in existence—they made specific recommendations, and then that was difficult to deal with because of first amendment problems, and we finally rationalized it by saying, "You have to look at the overall context of the whole publication." You know if that's all they do, then they obviously have to register; but if *Money Market* magazine has one column among fifty pages, or thirty pages, then that the overall tenor of the thing is not an advisory service. And that's how we dealt with it when I was Chief Counsel—I'm getting my chronology mixed up, but—but that's what it is.

KD: Well, speaking of chronology, let's jump back a little bit. You mentioned briefly Phillips and Loomis did the '66 study.

AR: Right. I am not sure how much Loomis did. Oh, there were a number of other people. And I did a little bit on it.

KD: Yes, I'd like to know a little bit about what really caused that to happen. What precipitated that study in '66?

AR: I think it could have been the Wharton study. But it was really a response to the enormous growth of the mutual fund industry.

KD: So how did the project work? You said you did a little bit of work with other people—

AR: Lou Mendelson drafted the part on advisory fees, and I remember sharing an office with him before I became Chief Counsel, when he was working on it. And he said, "What would you think if you found out that banks charged one tenth of one percent for managing trust funds? Or one percent. And the investment advisers to mutual funds charge a half of one percent. What would you think of that? I said, "I think that's outrageous." But that was the mindset that caused the thing to happen. Because if you look in the study, you'll find some things that illustrate that. As a matter of fact, one of the interesting things that happened at the hearings was, the Commission held up the Massachusetts Investment Trust as a model of management, because they didn't have an external adviser; they had trustees who got a salary, that I think was based somewhat on the size of the funds, but it was much less altogether than a half of one percent. And so at the hearings one of the senators or congressmen said, "You're holding up Massachusetts Investment Trust as a model, but you know when I look at the compensation of these directors, it looks like an estate, not an annual salary." And see that's the secret. And I always tell people, the reason why—and that's an insight—the reason why investment advisers can charge a half of one percent—although things have drastically changed, really drastically changed, because you need a large staff now, it's very expensive—and I'm not saying that a half of one percent is unreasonable. You know it depends. But at that time, the advisers were much smaller, most of them, and so it was easy to say: Oh, you got no break points. You're a Dreyfus. Dreyfus has a billion dollars and no break points. Massachusetts Investors Trust later externalized, and they set up an adviser company, which became the advisor to the funds, and it's Massachusetts Financial Services.

KD: They went the opposite way that what people would have expected.

AR: Yes.

KD: The '66 Study—how soon after that came out did there begin to be a push for legislation? Did it seem like cause and effect?

AR: I think that it followed naturally from the report because there were recommendations in the report.

KD: Did you testify or attend any of these hearings?

AR: I think I attended virtually all of the hearings.

KD: What was your function?

AR: Oh, just to listen and find out what was said, and to go back and to report, and to see what we should be doing. Oh, and also, very often—if you look at the record, you'll find this—very often someone, a senator or congressman, would say: Well, I want more details on this. I want you to write me a letter explaining all this in more detail. And so, I would go back, and I would help them write the letter. And as a matter of fact, it was the only case I have ever been authorized to send a letter to a congressional committee saying that someone had lied, because the fund of funds provision that Allan Mostoff did—I had very little, if anything, to do with it—that's Section 12(d)(1)—severely limits funds of funds. And because there was a pyramiding of fees, and there was a lack of transparency. Milton Mound had a fund called First Multifund, and he was very tricky because—I know a little bit about the '33 Act—under the '33 Act—the Act actually says if you file a registration statement it becomes effective within twenty days, automatically. But then the Commission felt that nobody really wanted to be caught making false statements or incomplete statements, so registrants filed the delaying amendments, and then the SEC formalized it even more, and you have a system for doing that. And Milton Mound was very clever. Milton Mound would file a registration statement, and he ignored all comments, and he just let them all become effective in twenty days.

KD: But in that twenty days he could do whatever he wanted to do.

AR: He actually had the nerve to file an exemptive application with the Commission that the Division vociferously opposed, and the Commission gave it to him. I even wrote a letter to the House committee—I signed my own name to it—it said, "You need to know that Milton Mound lied to you when he said so-and-so." Didn't do any good.

KD: Well, we're talking about the '70 hearings and the '70 legislation. And you'd talked about how it's been characterized as accomplishing little. How accurate is that?

AR: That's totally wrong. Totally wrong. It got us Section 12(d), and really severely limited pyramiding and lack of transparency. It got Section 36(b) that I think has put a check on grossly excessive fees. And it got a number of other things; it clarified a number of other things.

KD: What didn't it do? What are some of those things that one can say: Well, it didn't take care of this, it didn't take care of this.

AR: Well it didn't really take care of distribution fees.

KD: Is that 22—?

AR: That's Section 22(d) – no sales at other than a price described in the prospectus. There was a separate internal study on that. And the matter was handed over, ultimately, to NASD. At that time, there were two kinds of brokerage houses. There were NASD members that the NASD regulated, and non-NASD members that the SEC regulated. Ultimately, everybody had to register at the NASD. And when the SEC wanted the NASD to put a cap on distribution fees, because it was eight and a half percent in the front end—oh, I'll tell you something else that it did, but after I do this. The NASD said that it didn't have the authority, and I don't know who did the negotiations, probably somebody in the General Counsel's Office or maybe Market Regulation—said, "Nonsense. You have virtually plenary authority to regulate the conduct of your members, and you have the authority, and you're going to do it." And they did it.

KD: Didn't want the authority, I guess.

AR: Yes. Oh, another thing that the '70 Amendments did was kill what we then called front end load plans, but there was a kind of a plan, a periodic payment plan. And the periodic payment plan went something like this: You put in a minimum amount of money, and they took a half of it right off the top, and gave it to the dealers. And then you got a reduced load for the following years—maybe scaling down to seven percent, five percent. And the '70 Amendments killed that. And I'm not sure that we intended to kill it, I think we hoped to kill it, but we didn't realize how successful we'd be. But we did it in a way that no one really could object to, which was partly disclosure. You had to disclose a lot. And the one thing that said that we had to set up reserves to pay back the money if people redeemed.

And I will never forget—I think I put that in. I didn't draft it, but I had somebody put into the amendments that you had to have reserves for paying back fees. And I think Dick Phillips said, "Oh we tried that. It'll never fly." And so we put—but I think I persuaded him; we put it in. And of course, it flew like a horrible monster, because no one could do it. They didn't have the wherewithal to set up reserves—disclosure is bad enough.

KD: So that effectively got rid of front end loads.

AR: That got rid of all of those. And actually, you know what it was? It was a fund that invested in a single fund, and then charged additional distribution fees.

KD: A fund that invested in a single—

AR: In a single—like there was the Dreyfus Fund periodic payment plan, that invested in shares of another investment company, and the brokers would sell it. And then there was another type that we also killed that did pretty much the same thing. I forget what they called it.

KD: Now, following this legislation, is the process that the SEC then has to implement rules?

AR: Yes, we had to do rules. Actually, we did a series of—I think there's seven releases that my office and I drafted, that explained what a lot of it meant.

KD: How do you come up with that? Do you just sit around and think about it real hard, and put it down on paper?

AR: No, I mean there were complexities and ambiguities in the legislation, so we explained what it meant. They were very useful releases, because they did explain a lot of things, like the true meaning of Section 12(d)(1). That's the fund of funds thing, and some other things.

KD: Well the irony here is that as the mutual fund industry is really getting regulated in a fairly serious way, it's also running into some problems. There's a long period of net redemptions, starting in the early '70s. What did that context have to do with the way you handled things?

AR: Well I think that by that time—by the time they did the rule that allows money to be taken out of the fund to finance distribution—I was in the General Counsel's Office, and when I looked at it—oh, and incidentally, Divisions typically hate people in the General Counsel's Office who oversee their work; and so they determinedly keep me in the dark, until they sent their memo to the Commission. And so that was one of them. And when I finally saw it, I said to Dick Grant, who I think wrote the rule—

KD: Is this 12b-1? About distributions?

AR: Yes, 12b-1. I said, "This is terrible. You don't have any limits at all. There's not telling what would happen." Now, what happened—and what happened that I, at that point, never dreamed would happen was: People would charge a load, and then they would charge a 12b-1 fee on top of it. And I never thought that you could do that. And as a matter of fact, another one of my close friends, Allan Mostoff, was at Dechert then, and he did the first exemptive application that allowed the different types of shares to be sold—you know the A shares and the B shares, where you pay—where you pay in advance a higher fee, and then it scales down according to a fixed plan. He filed the first exemptive application for that.

KD: Getting back to the question here. Was there a sense that you needed to help out the industry that is not doing very well?

AR: Oh yes. They had been in net redemption, and so the SEC did the rule. The adopting release, but not the rule, has some criteria, which may have been suitable at the time, because it allows taking money out of the fund from people who have already paid a sales load, and won't pay any more. Is that in the best interest of the shareholders? And the answer then probably was, if you're in net redemption, yes, because it gets more assets into the fund, and with economies of scale you can make the thing go. But I think everybody—no one would disagree that those criteria don't make any sense. If it's been said once, it's said a hundred times, in several reports by a number of people—a number of organizations, including the Mutual Fund Directors Forum. I think they put that to the side though. It was too hard. But I think they're going to come up with—they're supposedly trying to come up with something now. And the SEC will re-examine the question. No, that was what happened. It's the old law of unintended consequences in full cry.

KD: Well something else that's happening at that point is that the banks are trying to get in.

AR: Yes, right.

KD: It seems to me that the SEC was essentially staying on the sidelines there.

AR: Not really. The SEC opposed the entry of the banks that were regulated by the sympathetic bank regulatory agencies, not the SEC. In any event, we ended up with Gramm-Leach-Bliley. And that was because the banks wanted to act as dealers, and sell fund shares. And there was a big struggle over that. And it ultimately—and there was an exemption in the Act for certain kinds of trust funds—mostly corporate trust funds, and other personal trust funds, that don't—those pools don't have to be registered under the Act. And the banks tried to get in under that, and the Commission and staff fought vigorously against that. As a matter of fact, under Hamer Budge, the SEC even sued Citibank, because Citibank put in an ad that said, in effect, come one, come all, we'll manage your money for a fee. And that case was settled. Oh, it turned out that when the Commission investigated—they had eight securities, and they aggregated them among the different trust funds in equal percentages. I guess there was some variation, depending on what the trust fund was. And so the Commission settled that. And then I remember—I guess when I was at General Counsel's office, there was another one that had a similar ad. I know Kathy McGrath wrote them a letter, and said, "You're out of your mind. If you do this, you have to register." So but that ended up with Gramm-Leach-Bliley, which as we speak, those rules are still being developed; because the Division of Market Regulation has to deal with bank regulators, and they're probably pushing it in one direction, and Market Regulation's probably pushing it in the other. And you know they have this limited number of trades limitation where the salesmen have to be registered representatives of a broker/dealer, and whether you have to have a separately registered broker/dealer, and on and on and on. And that's not even settled to this day.

KD: Right. It's been going on for a long time.

AR: Right.

KD: There's something I'm trying to put together. In '72—let's see—Congress asked the SEC to do a study on Section 22(d). At the same time, I see that you were involved in an industry advisory committee in '72. I'm wondering if those things were related at all.

AR: I have no recollection of that.

KD: Do you remember being on an industry advisory committee clear back at that early date?

AR: No, I don't. I just don't remember.

KD: Somebody named Danforth was involved.

AR: Oh, oh, oh. Oh sure, sure, sure. That was quite different from 22(d). I will tell you more than you want to know about that.

KD: Oh, excellent.

AR: Okay. This is really good. Yes, Danforth. It was an industry advisory committee, but it was not for the whole industry, it was just representatives of the industry. And what happened was: Chairman William J. Casey had found out that we had written letters to brokers saying, "You're trying to get people to put money in as free credit balances, or cash balances, and then you will use your discretion to invest those balances. And you have to register under the Investment Company Act." I remember the Division of Market Regulation thought this was peachy fine, and I had some disagreement with them on that. We finally prevailed. Casey was really bright. He was really clever. And so was Allan Mostoff. Casey said to Mostoff, "I think that with—"—and this is the infancy of computers—"I think that with computers now, you could do that. You could do some personalized services with a computer. And why don't you get together an advisory committee and see what you can work out?" Well, I thought—and I think they had already chosen the representatives. There was somebody from Merrill Lynch, there was somebody from Citibank, there was somebody from someplace else—I can't remember—and somebody from T. Rowe Price—and I think there was a fifth one, I can't remember. And we did write a report about it. And I thought: Oh, talk about putting the fox in the chicken coop. This is it.

KD: And one person from the SEC? Is that right?

AR: What?

KD: And you from the SEC?

AR: Right. Although I had somebody who was really smart. His name was Peter Sullivan. He was really smart. I couldn't have done it without him. And then later, Michael Berenson, who is now a partner of a firm here, who was working as—at first unpaid, and then later we hired him, because he came in and said, "I want to work for you, and I don't want any pay." It may not have been proper, but we did it. In any event, we went up to Danforth, who put ads in the paper that said, "Give me five thousand dollars, and I will give you personalized service."

KD: Who was Danforth?

AR: He was just some guy in some town in Connecticut. I forget where it was. But we knew who he was, and he was on the committee, and he was doing the ads. We had our eye out for him. So we went up there. And damned if he wasn't doing it. He was really doing it. And so then we had the counsel for Citibank, that we had sued. There's something called the Advisory Committee Act. And the Advisory Committee Act requires that the advisory committee have a charter, which is published and approved by the agency, maybe even by the Office of Management and Budget—I don't remember. And the Advisory Committee Act required that all meetings of an advisory committee be in public. Being these terrible government bureaucrats, we didn't want that. Well, fortunately, the Advisory Committee Act had about—I don't know—three or four months before it became effective, and we knew about it. And so we had to scramble to get the thing done before the Advisory Committee Act became effective. And we did it. And so we came out pretty much along the lines of what the Lowe case stands for, which is you have to do personalized service.

One of the things that was really difficult—really difficult—was, suppose you have a thousand people, and you do questionnaires, and you get the profiles of the people, what their needs are, and how much they should be putting—suppose you have a hundred people in this group, or maybe five groups—five different groups of a hundred people with slightly different answers to questionnaires, and suppose you run them all the same. Is that an investment company? And ultimately, although I teased somebody who represented Blackstone, that went on to greater glory—they own the world now—I talked to somebody who represented Blackstone, and he asked me that question, you know, suppose you had a number of people with the same profile, you ran them all the same way. And I said, "No. That's going to really kill your client, because you can't do that." But it didn't turn out that way.

KD: Well other things that changed the industry in the '70s: money markets, for example.

AR: Yes, right. Marty Lybecker ran that. We ultimately came out with a rule, 2a-7, which is the longest and hardest and most impenetrable rule you'll find, in certain respects. Marty Lybecker, who—I think he had been out teaching at Duke, and he came back to be an Associate Director of the Division. There were a number of exemptive orders for money market funds, because the question was, can you round up one dollar a share a penny? You know, penny rounding and amortized cost. The Commission had issued a number of exemptive orders. And finally when we had enough of them, we did a rule. Now the banking industry was really against this, and we had a series of hearings on that, about whether the Commission could allow money market funds. Because they were losing deposits, and the money market funds paid a lot more in return than the banks could, because there were regulatory limits. I think there was five percent on deposits, but money market funds in a time of inflation could pay more. You know they don't—they don't now, but I think they're approaching it again. So we had another fight, and we had a series of hearings on that. But we ultimately prevailed.

KD: I've got just a few more questions. Do you have more time?

AR: Okay, sure. Boy, I've been talking continuously.

KD: Money market funds. The other big thing that happened in the '70s was Vanguard revolutionizing the business. How did that affect the SEC's approach to all of this?

AR: Well I was heavily involved in that, because Vanguard had an exemptive order that the Commission ultimately granted, to allow an in-house funds of funds. In other words, if all of the funds in this fund of funds were funds that you were the adviser to, then you could have it. And I remember Aulana Peters was a Commissioner, and James Treadway. Anyway, I wrote a memo from the General Counsel's Office that whoever was General Counsel approved, that said that it was too soon to grant Vanguard an exemption. Congress had recently provided limits on funds of funds. And you couldn't just give it away. And moreover, we had serious doubts as to whether the Commission could exempt itself from the requirements of Section 12(d)(1), because they were allowing Vanguard to do something that—they were not enforcing the law, in giving this away. Aulana called me up and we talked about it. I wrote this memo from the General Counsel's Office, and she and Commissioner Treadway wrote a dissent, which by that time was unheard of—totally unheard of. Recently, in the corporate governance area, there have been severak dissents from the independent director, independent chairman rule, that have been published. But that was unheard of. They wrote a dissent from the Commission's Order, giving Vanguard the authority to do this. So I think it has changed a lot. But I don't think it's done any harm either, because there is transparency; there's reporting. You know what you're getting, and you're getting the prospectuses.

KD: So you moved into the General Counsel's Office then late '70s, working with Harvey Pitt and Ferarra

AR: Yes, right.

KD: I'm sure that you were doing more than just representing the Division of Investment Management. What were some of the issues that were pressing during that part of your career, going into the 1980s—the Reagan years?

AR: I wasn't representing the Division.

KD: You mentioned that Harvey Pitt liked to have people in there.

AR: Yes, right. But I was doing what Harvey wanted, and Ralph wanted.

KD: For example, the '80s is a time when we're getting—all the insider trader stuff is going on. Did that affect you?

AR: That was an enforcement function. There was also the business development company amendments, which I had a fairly large part in. I represented the Commission in that, in dealing with the industry. And Kathy McGrath, who had left the Commission, had a client who was very interested in having some relief from the—not insider trading, but insider transaction prohibitions of the Act—Section 17(d), Section 17(a). And so I negotiated some of the details of that legislation, which is also impossible to understand. That's why the—

KD: You must have understood it at one point.

AR: Well, no. Marty Lybecker wrote the stuff. It is so complicated no one used the amendments, except recently.

KD: This is the Business Development Company amendment.

AR: Yes, I think that's in '81. That's in '81, yes.

KD: Okay. All right. Anything else we should get on the record?

AR: No. Oh, I would tell you something I've said before, but I'll say it again. When I was Chief Counsel in the Division I had an interpretive principle, or rule, and that rule was: Would I like it if they did it to my mother? And I hope that some of that feeling may have carried over into my work at Dechert, because Dechert is a fine law firm, and the financial services group is a great group. And we always counsel people to follow the law. We may help them to expand an interpretation of it, but never over the line—I hope.

KD: What was behind your decision to come to Dechert? You came there right from the SEC, is that right?

AR: Oh, yes. I was approaching the age of 65, and I thought: Gee, I'd like to retire. I'll find out what my benefits are. I think I was making thirty-three thousand dollars a year, and I found out that it would be a little less than half. And I said: I got to get out of here while I still look like I can do something. And so I had always kept up with Allan Mostoff—we used to socialize. We went out to see—and I remember even the play, Brighton Beach Memoirs. It was that play about Brooklyn and Coney Island that was very popular. We went out to see this play, and I said, "Allan, I'm thinking of leaving the Commission." And he said, "Oh, we have to do something." And so we did, ultimately. It took a little while because the SEC was investigating one of Dechert's clients. We had to wait until they settled that.

KD: So you've been watching the SEC from the other side now.

AR: I was at the Commission for twenty-two years, and in September 2007, I will be here twenty-one years.

KD: Do you see the same Commission that you were working for all that time?

AR: Oh no. Oh no. Oh no, this is a Commission that—well I don't want to denigrate them, but this is a Commission that is not composed mainly of lawyers, as it was for many years. It is now composed of people who are more sympathetic to the industry and to business than the other Commissions were. And you know—and you can see it. You can see it in the tensions; you can see it in the corporate governance situation, where two Commissioners dissented, the Business Roundtable sued, and the Commission lost. And so it's a lot different. And you know I don't question their integrity, or their knowledgeability about the things that they're knowledgeable about; but it's an entirely different Commission.

KD: Yeah. Well times have changed, and to some extent the Commission has to as well.

AR: Yes. That's true. That's true.

KD: Well thanks very much for talking with me.

AR: Well thank you.

KD: It was a lot of fun.

AR: Oh good.