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June 21, 1976

AMERICAN
ENTERPRISE
INSTITUTE

MAYFLOWER HOTEL
WASHINGTON, D.C.

Somehow, two brief telephone conversations a long time ago, and weeks apart, one with Bill Baroody and the other with Mike Pertschuk, have me speaking twice today on the same subject within a two-hour period -- to the Senate Commerce Committee this morning and now here at lunch.

My first temptation was to give you the same words I offered the Senate this morning and you will see I yielded in great part to that urge.

My message before the Senate, as you will perceive in a few minutes, was:

- That some improvement in corporate behavior is now underway,
- That we should make only few precise changes in the law,
- That we should pay a little more attention to enforcing the laws already on the books, but
- That otherwise we should not get too excited about the whole thing.

I guess I still feel that way in the main, but I confess it's a bit disquieting to revisit the words of Professor Cary and others and be reminded of how really uncertain the state of corporate law still is. I was also sobered somewhat by Al Sommer's

statement in which he rather calmly accepts the notion of greater federalism in corporate affairs. In our five months together on the Commission I learned for one reason or another not to disregard his vote, rather, I should say his views, too easily.

I even dug out some old notes from a lecture I gave years ago to a Stanford Law School class where I was advocating a federal law that would prevent corporations from incorporating except in the state where its executive officers are normally located.

So, I will not dismiss the notion of more federal standards in the same cavalier fashion that I used when I first read Ralph Nader's treatise but I will say my own priorities do not place such laws high on the list of things to do.

My own perspective of what's primarily wrong with our large corporations does not call for major new federal legislation. Rather, it seeks a reorientation of existing agencies and organizations to continue a long and concentrated effort to change the manner in which our corporations are managed.

You will also see in my remarks the peculiar schizophrenia caused by being Chairman of a New York stock exchange company -- Chairman of the President's Regulatory Reform Task Force and Chairman of the SEC -- all in the same calendar year.

First, let me divide the subject into three simplistic parts:

Corporate behavior that is contrary to

law,

Corporate behavior that is contrary to

good business practices, and

Corporate behavior that is contrary to

someone's notion of good public policy

CONTRARY TO LAW

We do know that about 130 companies have made questionable or illegal payments here or abroad and the Commission has prosecuted 17 major cases to consent decrees.

The result in all seventeen cases has been to secure both a purging of past misbehavior and a change in the governance (accountability) to be reasonably sure that such misbehavior will not be repeated.

We conclude as a Commission that we have adequate remedies wherever we find concealed questionable payments, but we have suggested changes in the law which would put more pressure on management and the accounting profession to keep better records and public pressure on the New York Stock Exchange to give far more responsibility to outside directors.

Our efforts under existing law and our request for new laws are to create an internal reporting system that will place these rather difficult payment questions squarely before the independent directors, outside auditors and outside counsel.

In short, the recent revelations do not call for new federal standards, rather they show the need for a more effective reporting system.

The value of the existing system has just been validated by the work of our Enforcement Division over the past year.

The notion that our present system should be scrapped just when it has proved its worth would surely be an improper government response.

CONTRARY TO GOOD MANAGEMENT
PRACTICES

Would federal chartering cause our corporations to be managed better?

Well, I don't think so, but let's see if we can agree on what's wrong with management now.

- Too many boards are dominated by inside directors. Even where there are significant numbers of outsiders on a board, they are all too often old friends of the Chief Executive Officer who would rather resign from the board than severely criticize or vote to oust their old friend.
- Compensation for directors of too many large corporations is set at a figure which makes it apparent that no real work is expected.
- Information provided the boards of directors in too many cases is entirely the product of management and no effort is made and no authority is given to outside directors to make an independent investigation.

- Inside directors vote too often on salaries of employees, on questions of whether merger proposals should be accepted or on tender offers – all subjects that present some conflict of interest to management.

Directors seldom turn ineffective management out. As a result, stockholder democracy in most cases means simply the right to sell the stock.

Proposals for Reform

Companies limp along under poor management until either economic setbacks are so severe that change is compelled or until a large perceptive investor or company bids for stock control recognizing that the corporate assets can produce better profits.

To suggest, for example, that present corporate structures have been responsible for the worst combination of inflation and unemployment since the Depression is to ignore reality.

The more realistic conclusion is that management is too often complacent, self-perpetuating and unresponsive to legitimate shareholders' demands. When reported profits decline to such an extent as to threaten the serenity of their well paid isolation some managers are tempted to change the accounting, the figures or the morals of their company in order to present a more pleasing profit picture.

Proposals for Evolutionary Change

What is missing on too many boards is a truly independent character that has the practical capacity to monitor and to change management.

But, one must declare strongly that what is missing on some boards is present on others. We do have splendidly performing companies that have effective, responsive and responsible boards of directors.

As we look for solutions -- is it not far more sensible to move the poorly performing boards to the model of the successful companies, than to experiment with a system that has worked nowhere?

The essential first step is the creation of a panel of outside directors that will privately meet with the outside auditors.

Directors must be paid more and must spend more time on corporate business.

The independent members of the board must have some automatic method to secure information about operations.

The independent board members must also create some objective criteria of performance for management.

The independent board member must have exclusive jurisdiction to approve or veto decisions on certain types of issues such as salaries, merger proposals and selection of auditors, and the repurchase of corporate stock.

The question is whether "federal chartering" is the preferred way to secure this kind of needed independence.

I doubt it.

One survey shows that in less than five years the number of corporations with independent audit committees jumped from under 50% to almost 90%.

If the New York Stock Exchange does change its listing requirements to require independent audit committees with true authority, we will achieve a great deal.

We also know that there are many other major corporations experimenting with the role to be played by their boards. We can reasonably assume, therefore, that a better system of management accountability is coming.

FEDERAL CHARTERING

I suggested earlier, and I hope with some emphasis, that federal chartering will really not help maintain more lawful corporate behavior.

It is equally apparent, I trust, that federal chartering will not bring about better managed companies.

Who among you really would trust your investment dollar to directors who have an ill-defined obligation to an ambiguous public policy?

And, so, I am brought to the bottom line -- do we really want corporations to have a third duty? Should they be instrumentalities of public policies that are not set forth in statute?

It is tempting to put public interest directors on a board, to speak for employees, for environment, for a better life!

It is admittedly difficult for Congress to balance between needed economic growth and environmental improvement -- between the need for profits and the desire for safe products and working conditions.

Why not put the hassle on the boards and make them get board members who have the broader public interest at heart?

My simple answer is that it will not work! Raymond Vernon discussed the evolution of similar considerations in Europe.

“Public policy had been parcelled out among committees, organizations and enterprises throughout the society . . . and the result . . . has been a growing tendency to use large national enterprises to solve specific problems as if they were agencies of the state. And, there has been a related tendency to develop methods of government that have reduced the role of the parliamentary process and elevated the role of specialized groups.”

In sum, when we have tried to make corporations instruments of government policy, they become less efficient and the government becomes less democratic.

My views of American business today is that while a lot of major companies have failed their stockholders and the public, a lot more have devised methods of governance that make their management truly accountable to independent directors who are responsible.

Our effort should be to raise the standard of business leaders to that of those who are doing the job quite well. Only if we fail to make steady progress should we force a greater federal intrusion into business management.

Frankly, I am far more concerned about the ability of our corporations to raise equity capital than I am about whether we can raise the level of management conduct.

Our dramatic trend toward a debt-based industrial complex rather than the equity-based industry of 25 years ago strikes me as our most critical corporate problem.

As we lean to debt we lose the flexibility and the innovative growth critical both to capitalism and to our democratic society.

I have no doubt of our capacity to raise the standards of management behavior - and I see clear progress. I am less optimistic about our ability to redress the debt/equity ratios. Surely we should be as concerned about the erosion of capitalism as we may be impatient about the slowness of our moral advancement.

I confess a great concern for the sometimes strident but always impatient call for change now!!

I also confess a great affection for words written by a San Franciscan longshoreman in the 1960's. Eric Hoffer said then:

“If one were to pick the chief trait which characterizes the temper of our time, it would be impatience. Tomorrow has become a dirty word. The future is now, and hope has turned into desire.

* * * *

The better part of statesmanship might be to know clearly and precisely what not to do, and leave action to the improvisation of chance.”

The “chance” of “Watergate” gave us a better government and began a series of corporate investigations that has already improved our vision and raised corporate behavioral standards.

I suggest a steady and cautious course as we pursue further improvements that will not needlessly interfere with the preservation of the capacity of our business community to maintain innovative growth.

At stake is not merely the profits of business, but the economic freedom upon which our form of democracy is dependent!!