April 10, 1995

The Honorable Steven M. H. Wallman
United States Securities and Exchange Commission
450 Fifth Street, N. W.
Washington D.C. 20549

Dear Commissioner Wallman:

Thank you for sending the materials from the March 6, 1995 meeting of the Advisory Committee on the Capital Formation and Regulatory Processes (Advisory Committee). I found the information interesting and thought-provoking. I appreciate this opportunity to provide the following comments on potential enhancements to the existing system of capital formation in the United States.

Let me begin by emphasizing my belief that the capital markets in the United States represent one of the most effective and reliable markets in the world. Investors readily provide capital resources that are allocated efficiently and effectively to supply capital to enterprises. The integrity of this capital market builds upon a foundation of issuers providing a sufficient amount of relevant and reliable information to investors. The Securities and Exchange Commission (Commission) serves a vital regulatory oversight role to ensure that issuers, auditors and others provide this information to investors.

The principal tools utilized by the Commission, the Securities Act of 1933 and the Exchange Act of 1934, have served the capital markets well these past 60 years. The strength of our current capital market serves as a testament to the existing securities legislation, related regulations, and interpretations. A lot has happened since the introduction of this legislation, however. The existing regulatory scheme for the registration process requires an overhaul to address changes that have occurred in the global (and more competitive) marketplace and to foster the continued leadership of the United States capital markets.

Competitive pressure on today's enterprise requires increasing efficiency in all aspects of business, including capital formation and application. The continued explosion of global communications and information processing has created demands for cycle time reduction migrating towards a virtually real-time business (and information) environment. The continued expansion of capital markets beyond the additional geographic boundaries on a map has opened the door to a global capital marketplace. Although this increased level of competition for existing capital resources may be detrimental to those who are ill-prepared to compete on a global scale, it provides investors with more opportunities for optimal returns.

To meet these changes, enterprises in the 1990's and beyond are likely to require increasingly quicker access to capital when the marketplace is advantageous. The challenge
facing us in this environment will be how to balance the seemingly contradictory goals of protecting the investor through maintaining integrity in the marketplace and remaining competitive on a global scale with the efficient and effective allocation of capital. The current system requires significant changes to balance these needs and to compete in a global marketplace in the future. These changes are likely to include how to compile and present financial information to explain resources and changes in resources, what financial information will be most important to capital providers, and the frequency, timeliness, and manner of delivery of information.

The manner to accomplish regulatory oversight in this changing environment remains unclear. Clearly, regulatory involvement has been effective in establishing the current credibility of our markets. The continued involvement of regulatory oversight appears essential to maintaining that credibility. In any event, the Advisory Committee should quantify the cost of various forms of regulatory oversight and should compare these costs to the benefits derived. These costs and benefits may not be restricted to monetary measures. They include concepts that extend beyond typical cost-benefit analyses like the value of public trust, the benefits from expanded disclosures, and the cost of delayed capital availability. Nevertheless, we should begin to measure the economic costs and benefits of regulation. The Advisory Committee should explore developing the information suggested in the March 7, 1995, letter to you from Robert Elliott as a foundation for this analysis.

The Advisory Committee identified one potential method of increasing the access time to capital markets by migrating from a transactional-based disclosure system to a company-based continuous disclosure system. The progress achieved in the development of computer networking capabilities, data transmission and manipulation, and information technology in general is providing an environment where a company-based model may be feasible, at least for some registrants. What better information could be available to an investor than current information in a format that the investor chooses to best meet his or her needs? The company-based model could benefit both investors and issuers. Larger, more sophisticated investors as well as smaller, retail investors would benefit since the issuer could provide increased access to user-tailored information for the organization more frequently. The company-based model could convey information regarding the issuer’s business, operating results, capital requirements and liquidity as well as expected capital needs and funding sources similar to that accessible more slowly today. The benefit to the issuer is a greater degree of flexibility and quicker access to capital sources. Inherently, that translates to a reduction of the “cost” of capital and an increase in the efficiency of the market.

In addition, existing degrees of segregation between the type and sophistication of the investor may continue to diverge resulting in vastly different information requirements for different investors. The development of alternative sources of capital (the public versus private markets) was the market’s response to the perceived costs of capital under the existing regulatory framework. This is representative of an efficient and adaptable marketplace’s developing alternatives to optimize capital formation. The creation of alternatives provides opportunities for issuers to customize a package of capital that best meets the issuer’s needs at a given time. The Commission should foster the continued development of capital alternatives since the result is beneficial to both the capital user and provider. These efforts should continue so long as different sources of capital increase the efficiency of the market and the timeliness of the distribution of capital at a reasonable cost. The Commission should minimize the effect of regulatory inhibitors like the integration test and general solicitation requirements that create conflict between alternatives. Although the concerns addressed by these provisions are warranted in certain circumstances, the effect of these provisions should be limited only to those circumstances deemed to be absolutely
critical to protect the investor so that the flexibility of the issuer to attract capital through the 
best alternative available can be maximized.

These advancements may significantly increase the opportunity for mistakes or 
manipulations that degrade the reliability of information provided to investors, however. 
one strength of the current system is the reliability achieved as a result of auditor 
involvement, the regulatory role in securities registrations, and the due diligence procedures 
performed by underwriters and attorneys. The participation of these professionals in the 
capital formation process provides the investor with a necessary corroboration of 
information provided by enterprises seeking capital. A goal of any system must be to 
continue to provide reliable information with adequate remedies to the investor when 
reliability is compromised. At the same time, the ability of experts and underwriters to 
fulfill their responsibilities without incurring unreasonable expense is critical to a cost-
efficient allocation of capital. I do not perceive significant limitations on the ability of 
underwriters and experts to conduct due diligence procedures in a company-based 
environment. The timing of performing due diligence procedures may be shifted, 
however. Procedures may be conducted on a "round-the-clock" basis to meet the needs of 
a company-based reporting system. This type of continuous involvement by underwriters 
and experts may in fact increase the effectiveness of due diligence procedures in the 
registration process.

The recommendations of the Jenkins Committee, the charter of the Elliott Committee, and 
the objectives discussed in the Background Paper focus on the changing environment and 
the need to continue to revisit existing procedures and information in light of new 
requirements. Like most things, significant change is a process that occurs over time. The 
problem is that "time" is compressed greatly today and competitors to U.S. capital markets 
are not standing still. We must continue to investigate methods to re-engineer and improve 
the capital markets to remain a leader in capital formation and distribution in a world 
marketplace... I support the Advisory Committee's efforts in this area.

Sincerely,

Michael A. Conway

cc: R. K. Elliott - KPMG
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