

Y 4
. In 8/4
95-2

1019

95-2
In 8/4
95-2

SEC AUTHORIZATION OF APPROPRIATIONS

GOVERNMENT

CUMENTS

Storage

MAY 10 1977

FARRELL LIBRARY
KANSAS STATE UNIVERSITY

HEARING

BEFORE THE

SUBCOMMITTEE ON CONSUMER PROTECTION AND FINANCE

OF THE

COMMITTEE ON

INTERSTATE AND FOREIGN COMMERCE

HOUSE OF REPRESENTATIVES

NINETY-FIFTH CONGRESS

FIRST SESSION

ON

H.R. 3721 AND H.R. 3722

BILLS TO INCREASE THE AMOUNT AUTHORIZED TO BE AP-
PROPRIATED FOR THE SECURITIES AND EXCHANGE COM-
MISSION FOR FISCAL YEAR 1977 AND SPECIFIED AMOUNTS
FOR FISCAL YEARS 1978-80

MARCH 10, 1977

Serial No. 95-2

Printed for the use of the
Committee on Interstate and Foreign Commerce



U.S. GOVERNMENT PRINTING OFFICE

WASHINGTON : 1977

87-331

KSU LIBRARIES

006920
A11900 816920

COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE

HARLEY O. STAGGERS, West Virginia, *Chairman*

JOHN E. MOSS, California
JOHN D. DINGELL, Michigan
PAUL G. ROGERS, Florida
LIONEL VAN DEERLIN, California
FRED B. ROONEY, Pennsylvania
JOHN M. MURPHY, New York
DAVID E. SATTERFIELD III, Virginia
BOB ECKHARDT, Texas
RICHARDSON PREYER, North Carolina
CHARLES J. CARNEY, Ohio
RALPH H. METCALFE, Illinois
JAMES H. SCHEUER, New York
RICHARD L. OTTINGER, New York
HENRY A. WAXMAN, California
ROBERT (BOB) KRUEGER, Texas
TIMOTHY E. WIRTH, Colorado
PHILIP R. SHARP, Indiana
JAMES J. FLORIO, New Jersey
ANTHONY TOBY MOFFETT, Connecticut
JIM SANTINI, Nevada
ANDREW MAGUIRE, New Jersey
MARTY RUSSO, Illinois
EDWARD J. MARKEY, Massachusetts
THOMAS A. LUKEN, Ohio
DOUG WALGREN, Pennsylvania
BOB GAMMAGE, Texas
ALBERT GORE, Jr., Tennessee
BARBARA A. MIKULSKI, Maryland

SAMUEL L. DEVINE, Ohio
JAMES T. BROYHILL, North Carolina
TIM LEE CARTER, Kentucky
CLARENCE J. BROWN, Ohio
JOE SKUBITZ, Kansas
JAMES M. COLLINS, Texas
LOUIS FREY, Jr., Florida
NORMAN F. LENT, New York
EDWARD R. MADIGAN, Illinois
CARLOS R. MOORHEAD, California
MATTHEW J. RINALDO, New Jersey
W. HENSON MOORE, Louisiana
DAVE STOCKMAN, Michigan
MARC L. MARKS, Pennsylvania

W. E. WILLIAMSON, *Chief Clerk and Staff Director*

KENNETH J. PAINTER, *First Assistant Clerk*

ELEANOR A. DINKINS, *Assistant Clerk*

Professional Staff

LEE S. HYDE
ELIZABETH HARRISON
JEFFREY H. SCHWARTZ
BRIAN R. MOIR
KAREN NELSON

MARGOT DINNEEN
ROSS DAVID AIN
CHRISTOPHER E. DUNNE
WILLIAM M. KITZMILLER
MARK J. RAABE

THOMAS M. RYAN

NANCY A. NORD, *Minority Staff Assistant*

SUBCOMMITTEE ON CONSUMER PROTECTION AND FINANCE

BOB ECKHARDT, Texas, *Chairman*

RALPH H. METCALFE, Illinois
ROBERT (BOB) KRUEGER, Texas
CHARLES J. CARNEY, Ohio
JAMES H. SCHEUER, New York
THOMAS A. LUKEN, Ohio
HARLEY O. STAGGERS, West Virginia
(*ex officio*)

JAMES T. BROYHILL, North Carolina
MATTHEW J. RINALDO, New Jersey
SAMUEL L. DEVINE, Ohio (*ex officio*)

JANIE KINNEY, *Counsel/Staff Coordinator*

FRANZ F. OPPER, *Counsel*

(II)

CONTENTS

	Page
Text of—	
H.R. 3721-----	3
H.R. 3722-----	4
Statements of SEC witnesses—	
Hills, Hon. Roderick M., Chairman-----	5
Haynes, Lawrence H., Comptroller-----	5
Sporkin, Stanley, Director, Division of Enforcement-----	5
Additional material submitted for the record by SEC—	
Exhibit A—Securities and Exchange Commission estimated budget requirements for fiscal years 1977-80-----	11
Table showing the breakdown of minorities and women employed by SEC-----	13

CONTENTS

1. Introduction

2. The Law of the Sea

3. The Continental Shelf

4. The Exclusive Economic Zone

5. The High Seas

6. The Deep Seabed

7. The Law of the Sea Convention

8. The United Nations Convention on the Law of the Sea

9. The International Law of the Sea

10. The International Law of the Sea

SEC AUTHORIZATION OF APPROPRIATIONS

THURSDAY, MARCH 10, 1977

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON CONSUMER PROTECTION AND FINANCE,
COMMITTEE ON INTERSTATE AND FOREIGN COMMERCE,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10 a.m., in room 2322, Rayburn House Office Building, Hon. Bob Eckhardt, chairman, presiding.

Mr. ECKHARDT. The subcommittee will be in order.

Today, the Subcommittee on Consumer Protection and Finance holds hearings on two bills, H.R. 3721 and H.R. 3722. H.R. 3721 would provide a supplemental authorization to the Securities and Exchange Commission of \$1.5 million, increasing its total authorization for fiscal year ending October 31, 1977, to \$56.5 million. This additional amount is necessary to meet the costs of last October's cost-of-living pay increase, the recent executive salary raise, and to provide funding for the agency's urgently needed ADP and recordkeeping systems.

H.R. 3722 provides authorizations for each of the succeeding fiscal years. Beginning in fiscal 1978, these authorizations would be \$64 million, \$70 million, and \$78 million.

I find one thing particularly puzzling and, from the point of view of the protection of the public investor, quite disturbing about the requested future authorizations. That is that the submitted budget does not provide for any increase in the size of the Commission's enforcement staff.

The general objective of the Federal securities laws administered by the Commission is to protect the interests of the public and investors by preventing fraud, deceit, and manipulation in the sale and trading of securities. It is critical to the achievement of this objective that the enforcement program be able to effectively carry out its mission.

In 1972, the report of the Advisory Committee on enforcement policies and practices—generally referred to as the Wells Committee report—acknowledged that an effective program of securities industry regulation was dependent upon an effective enforcement program. It recommended that the Commission's enforcement staff be doubled. This objective has never been reached. As a matter of fact, the Commission's Enforcement Division, which is presently undermanned, has had a number of new demands upon its resources which were never envisioned by the Wells Committee.

To mention a few of these areas, I think first of all, it is pretty clear that the market surveillance capability of the staff ought to be greatly enlarged, particularly in the rapidly growing trading in options.

The options area spans the current trading in call options, to dual marketmaking in both options and the underlying securities, to future trading input options. Surveillance of options trading will have to be closely coordinated with surveillance of trading in the underlying securities, particularly where the underlying securities are traded on a different market.

Under the Securities Act Amendments of 1975, the Commission was given for the first time regulatory responsibility for municipal securities dealers and for some 2,400 transfer agents. As banks move more aggressively into the retailing of traditional securities, an increasing number of enforcement problems can be expected to result in that area. In addition, during the past few years, there has been a remarkable growth in cases requiring substantial accounting expertise, including tax shelter frauds, insurance accounting, real estate investment trusts, and the numerous and far-reaching illegal foreign and domestic payments.

As a result of the Commission's enforcement efforts, particularly its organized crime unit, it is estimated that at the beginning of 1978, the Commission will have some 300 criminal reference reports pending before the Department of Justice, triple the number pending in 1974.

Layered upon the foregoing has been the perceived recent tendency of respondents to litigate with the Commission, rather than to settle their cases prior to actually going to court. Because of their complexity, the resulting trials tend to be lengthy and to require a substantial allocation of the Enforcement Division's time and resources. Finally, that very important and necessary adjunct to SEC enforcement—the private right of action under the securities laws—has been severely restricted by a number of recent Supreme Court cases. Accordingly, a very substantial additional burden has been placed upon the Commission's facilities to pick up the enforcement slack which had been previously assumed through private litigation.

The Commission's enforcement effort is its backbone. It is the principal vehicle for protecting the small investor and in generating investor confidence in our securities markets. The effectiveness with which the Commission has carried out its mandate is reflected in the fact that the U.S. securities markets are the most attractive and highly regarded in the world. I am concerned that any attempt to diminish the Commission's enforcement effort will largely eviscerate the effectiveness of the Commission and have a concomitant adverse effect upon our securities markets.

Today, I am hopeful that in discussing the Commission's authorization request, Chairman Hills will address the issue as to why, in light of the Wells' recommendations and the increased demands upon the enforcement staff, the Commission's budget for 1978 provides for virtually the same number of Enforcement Division personnel as in 1975, and actually reduces the number of enforcement personnel in the regional enforcement offices from the 1975 level.

Without objection, the text of H.R. 3721 and H.R. 3722 will be placed in the record at this point.

[The texts of H.R. 3721 and H.R. 3722 follow:]

95TH CONGRESS
1ST SESSION

H. R. 3721

REPRODUCED FROM
OFFICIAL RECORDS

IN THE HOUSE OF REPRESENTATIVES

FEBRUARY 21, 1977

MR. STAGGERS (for himself and Mr. DEVINE) introduced the following bill;
which was referred to the Committee on Interstate and Foreign Commerce

A BILL

To amend the Securities Exchange Act of 1934 to increase the amount authorized to be appropriated for the Securities and Exchange Commission for fiscal 1977.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*
3 That section 35 of the Securities Exchange Act of 1934
4 (15 U.S.C. 78a et seq.) is amended by striking the amount
5 "\$55,000,000" before the words "for the fiscal year ending
6 September 30, 1977" and inserting in lieu thereof the
7 amount "\$56,500,000".

I

95TH CONGRESS
1ST SESSION

H. R. 3722

IN THE HOUSE OF REPRESENTATIVES

FEBRUARY 21, 1977

Mr. STAGGERS (for himself and Mr. DEVINE) introduced the following bill;
which was referred to the Committee on Interstate and Foreign Commerce

A BILL

To amend the Securities Exchange Act of 1934 to authorize specified amounts to be appropriated for the Securities and Exchange Commission for fiscal years 1978-1980.

- 1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*
3 That section 35 of the Securities Exchange Act of 1934 (15
4 U.S.C. 78a et seq.) is amended by striking the words "and
5 not to exceed \$56,500,000 for the fiscal year ending Septem-
6 ber 30, 1977. For fiscal years succeeding the 1977 fiscal
7 year, there may be appropriated such sums as the Congress
8 may hereafter authorize by law" and inserting in their place
9 the following: " , \$56,500,000 for the fiscal year ending
10 September 30, 1977, \$64,000,000 for the fiscal year ending

- 1 September 30, 1978, \$70,000,000 for the fiscal year ending
- 2 September 30, 1979 and \$75,000,000 for the fiscal year
- 3 ending September 30, 1980. For fiscal years succeeding the
- 4 1980 fiscal year, there may be appropriated such sums as
- 5 the Congress may hereafter authorize by law”.

Mr. ECKHARDT. Today we are pleased to have you, Mr. Hills, the Chairman of the Securities and Exchange Commission. I understand you are accompanied by Mr. Haynes and Mr. Shipman.

Are they both here?

Mr. HILLS. That may be my mistake, Mr. Chairman. Mr. Shipman has left the Commission as Executive Director. It was my understanding that it would not be necessary for him to fly down from New York for the hearing.

Mr. ECKHARDT. That is perfectly all right. Mr. Lawrence Haynes is with you today.

Mr. HILLS. Yes.

Mr. ECKHARDT. You may proceed, Mr. Chairman, as you desire.

STATEMENT OF HON. RODERICK M. HILLS, CHAIRMAN, SECURITIES AND EXCHANGE COMMISSION, ACCOMPANIED BY LAWRENCE H. HAYNES, COMPTROLLER; AND STANLEY SPORKIN, DIRECTOR, DIVISION OF ENFORCEMENT

Mr. HILLS. If I may, I would dispense with reading the prepared statement we have provided your staff. Of course I would be glad to answer any questions about it.

As an overview, I think it is important to note that during the past 17 months we have engaged in as detailed and careful and thorough an overhaul of our procedures as possible to make the Commission more modern. In fact, to answer the questions you have raised, I have to put in this background.

There were a number of things about the Commission that were quite out of date. It has been said that if we had found any Wall Street houses to have back offices performing the way our back offices perform, we would have shut them down. We simply did not have easy access to material in our files.

There are some 11 million pages a year filed with us, 150,000 individual filings. We had nothing but a manual system to get those back into our hands, and we had no method of accumulating material from them. We had no real system for using them for statistical work. So we decided 17 months ago to begin a modernization program within the Commission.

I think the principal answer I have as to why we have not requested additional personnel is that in order for the Commission to function properly and effectively to take advantage of the information and expertise that we have, we must be able to communicate with ourselves better and to make better use of our materials.

We will, by 1978, have an efficient computer system that will give us random access to our files. It will give us at least an embryonic early warning system so that we can best use our assets and our people. It will allow all of our regional offices to have access to our files. It will make it possible for the Commission to integrate its own work in a better fashion.

More important, it will make it possible for us to divert our present budget from clerical people, from people who do not directly affect the enforcement activities of the Commission, into the frontline activities of the Commission. It will reduce substantially the number of people in our records section freeing up those resources.

We have begun and are about 75 percent completed with a division-by-division, region-by-region personnel analysis, looking at whether our people are being used effectively, making recommendations to each of the division directors, and each of the division administrators to, again, make the Commission more efficient in how we use our time.

I think that there are two tests that are important here in judging whether we have the capacity to do the job given us by the Congress. One, of course, is are we doing it? What does our work product look like?

I am proud of that product. I think that without question there is no other agency able to do a better job to enforce with vigor the laws that are entrusted to it to enforce.

In other words, I believe that the statement that the Securities and Exchange Commission does a better job of maintaining compliance with the laws that are its responsibility than any other governmental agency is a fully accurate statement.

So I think that on the objective test we are doing our job. The second test relates to our size. It is terribly important for an agency like the SEC to stay small. It is terribly important that it be efficient. An agency like the SEC is only as good as its people. We can maintain the quality of people that we have at our agency at about our current size. We can do a very good job of attracting the very best people in Government.

Again, I know of no other Government agency that consistently has as high a calibre of people applying for jobs and being hired.

Now to the specifics. It is, of course, not only the enforcement division that deals with such matters as puts and call options and market regulation. We have another division, the Division of Market Regulation that is primarily responsible for designing rules for creating the surveillance systems within the Commission. It is the Market Regulation Division that has to put the rules in place that must be followed. The enforcement division primarily looks after the violations of the rules.

We have been busy indeed this past 18 months in creating the rules and dealing with the structure of the market. The market structure in itself is in a state of flux. The chairman knows, as well as anyone,

not only are we moving toward a national market system, that not only have we changed the rules in respect to offboard restrictions on trading in New York exchanges, and not only do we have dual trading in options and stocks; but we also have all kinds of other changes underway.

As recently as yesterday, the voluntary organization called the National Market Association came up with an outline of a new information system that would connect all of these exchanges and which will be terribly material, among other things, in detecting violations of our laws.

During this past year we have created a Directorate of Economic and Policy Research to give us the capacity to engage in economic analysis of how the market works, to make a decision as to what kind of conceptual framework our regulations should apply, to know best how to do it.

We are in a very difficult information-gathering stage, full of pitfalls in our examination of stock trading, new marketmaking, over-the-counter marketmaking, all of those things that the chairman so accurately points out have come upon us with an unusual ferocity during this past year or two.

I believe we have moved in every area with a great deal of vigor. A few weeks ago, as we moved in the options area, it became apparent to me and Mr. Sporkin that we did indeed need more people. We made the money available to hire more people.

I must say that the present freeze that has been imposed by the Administration may interfere a little bit with putting people into the surveillance and options areas. But my judgment right now is that we can go ahead there without additional manpower.

I think the test, Mr. Chairman, is do we have the resources and reserves to meet the problems that we have? The answer to that question, I can say to you, is "yes," although we have some problems. The principal problem is that we do not know enough about what we are doing and for that reason we have a rather sophisticated tracking system which Mr. Sporkin has just recently put into effect at our Washington regional office and our Seattle regional office. This system will give us far more information about what our people are doing and where they are doing it. It will give Mr. Sporkin a far better capacity to know what his people are doing.

In terms of litigation, which the chairman also accurately points out is increasing, we have just engaged in a contract with the Columbia law school to create a very sophisticated training technique for our trial lawyers that will be fashioned after, and, indeed, run by the people at Harvard Law School who have done this for years at Boulder, Colo., and I think I am right in saying we are going to send 40 lawyers to that training session for 3 weeks and it will cost us, what? \$8,000.

Mr. HAYNES. Yes.

Mr. HILLS. Stan's people are also involved in a sophisticated computer program to develop better trial techniques to retrieve information to improve our capability of dealing with the larger cases.

We have recently initiated a rejuvenated attorney-fellows program, in which we are bringing sophisticated corporate lawyers from private industry into the Commission for a 2-year period. These will be people of the very highest quality. One of the people we will hire is

a former law clerk of Justice Douglas on the Supreme Court who has had 5 or 6 years of intensive experience.

These people will come into the General Counsel's office to make our place more efficient. Most of all, we will rely more than we have, even in the past, upon the self-regulatory organizations which are so important to our system. The genius of the securities system in this country is its reliance on the efficacy, integrity, and capacity of the self-regulatory organizations, not only the stock exchanges but also organizations like the organized bar, the AICPA, the Financial Accounting Standards Board. It is our capacity to make those people understand their responsibilities and do their jobs that makes it possible for the Commission to fulfill its mandate.

Just yesterday, the Commission approved an enormous initiative by the New York Stock Exchange. It perhaps is not as complete as we would all like, but it is an enormous first step. As a requirement to be listed in the New York Stock Exchange, members will be required to create audit committees of outside directors that have no conflicts of interest. This will give an independent character to every listed company on the New York Stock Exchange.

Now as you go back over the sad history of questionable payments that have occupied the headlines and occupied so much of our time, you will see, first of all, that the Commission has been able to do an enormous job, far beyond its own resources, by entering into consent decrees whereby the corporations utilize outside counsel approved by us and outside directors approved by us to study and report on what payments problems they may have had.

Most of you have seen Gulf Oil and some of the other reports coming in. The Lockheed report is being carried on by a very competent, retired Federal judge, guided by independent directors who are new to Lockheed.

As I recall, the Gulf Oil report cost Gulf Oil about \$2 million.

Mr. SPORKIN. \$3 million.

Mr. HILLS. I was told that the Firestone outside audit report is going to be of the same character. In a sense we spent as much as \$20 or \$30 million more than our budget last year in the questionable payments area, using the technique of a federally mandated outside audit committee, which is essentially doing work directly for the benefit of the stockholders.

We have recently proposed to change our rules to require that companies have adequate systems of internal control. Here, too, recognizing that we are putting a burden on business, we are indeed increasing the capacity of the Securities and Exchange Commission to enforce the securities laws.

Finally, Mr. Chairman, I have to tell you that I cannot answer the question completely. I do not know whether we have enough resources. I cannot tell whether we have enough resources until we have finished the zero-based budgeting analysis that we had begun some time ago.

I can't tell you whether we can do it until we have completed the early warning systems and until the tracking systems are in place and fully developed.

I do not know what the surplus resources of the Commission will be one year from today because I do not know precisely how the modernization program will develop.

Conceivably, at this time next year we will have as many as 30 or 40 extra slots at the Commission which can be diverted to enforcement, general counsel, or market regulation, as we modernize the Commission.

Today, I can tell you that if anybody in the Commission, including Mr. Sporkin, comes to me and says he needs another lawyer for something, we can provide that lawyer. If market regulation comes to us and says, "We need some more money for Lexitron gear," or something else, we have some extra money for doing that. We have developed the capacity to respond to these problems.

However, I think it is fair to say that our effectiveness depends largely upon the willingness of our Enforcement Division, and of all of the people in the Commission, to work overtime. We are able to do our job well primarily because we have more, I think, than any other agency, dedicated people of high capacity who care willing to do a job beyond the average job that is done in Government.

Thank you.

[Chairman Hills' prepared statement follows:]

STATEMENT OF RODERICK M. HILLS, CHAIRMAN, SECURITIES AND EXCHANGE COMMISSION

Mr. Chairman and members of the Subcommittee, I want to thank you for this opportunity to testify in support of H.R. 3721, and H.R. 3722, both of which involve authorizations for the Commission's budget. I also want to express our appreciation for the Subcommittee's consideration in scheduling this legislation for hearings so promptly. Both bills are, as you may well appreciate, of great importance to the continued efficient functioning of the Commission.

The first of these bills, H.R. 3721, would increase the Commission's budget authorization for the current fiscal year from the existing level of \$55 million, to a new ceiling of \$56.5 million. This increase is needed in order to accommodate additional appropriations that have become necessary since our fiscal 1977 budget authorization was established, nearly two years ago.

Mr. Chairman, Exhibit A attached to my statement tabulates the figures that comprise our increased budgetary requirements, and I submit it for inclusion in the hearing record.

The Commission was originally appropriated \$53 million for the current fiscal year. However, the mandatory, governmentwide pay increase of last October added approximately \$2.4 million to our fiscal year 1977 payroll costs and that amount will be added to our appropriation through legislation submitted by the Office of Management and Budget in behalf of all Federal agencies. This amount alone would place our appropriation some \$400,000 over our authorized ceiling.

Added to that is the cost of the recent executive pay increase, which is also mandatory, and which will add some \$230,000 to our payroll costs for fiscal year 1977.

And finally, the Commission is seeking a supplemental appropriation for fiscal year 1977 in the amount of \$880,000 in order to meet expenses which could not have been anticipated, and which cannot be delayed without serious, adverse repercussions.

These three items total \$3.5 million and would bring our total appropriation for fiscal 1977 to \$56.5 million. That is, of course, \$1.5 million more than our current authorized ceiling, and the reason we are seeking enactment of H.R. 3721.

Mr. Chairman, at this point I would like to explain more fully the need for the \$880,000 supplemental appropriation which I previously mentioned. I want to stress again that this is the absolutely rock-bottom amount needed for continued, efficient operation. The bulk of it, \$676,000, will go to assuring continued progress of the Commission's program to modernize our automatic data processing (ADP) and records system. Of that amount, \$400,000 is for the records systems, and \$276,000 is for ADP.

This modernization began last year after the Commission sought, with the concurrence of the Office of Management and Budget, \$900,000 in order to initiate the program. That amount was appropriated as part of our fiscal year 1977 budget, and since then we have made substantial progress in planning both the conversion of official public files to micro-fiche and high-reduction film and pro-

viding support and improvement in record handling, storage and retrieval. In the ADP area, we hope to soon complete an analysis of the Commission's information systems requirements, to replace our present antiquated system with a modern high capacity computer facility, and to further train ADP staff in advanced computer applications.

Mr. Chairman, when we originally sought \$900,000 to begin this program, we felt that the Commission could efficiently continue to carry out its responsibilities under the Federal securities laws only if its systems were upgraded, internal procedures were streamlined, and its analytical capabilities were improved. Today, more firmly convinced than ever of this need, we have produced a five-year plan designed to accomplish those goals, and are urgently in need of this supplemental appropriation in order to continue the progress we have begun. I will discuss this program in greater detail later in my testimony when I deal with the Commission's authorization request for fiscal years 1978, 1979, and 1980.

The balance of the \$880,000 supplemental we are seeking for the current fiscal year is comprised of the following: \$120,000 to pay utility charges incurred outside regular operating hours; \$47,000 to pay increased charges for the Federal Telecommunications System; and \$37,000 for travel expenses of the National Market Advisory Board. Of these items, I would point out that the first two—additional utility and telephone charges—were imposed by the General Services Administration well after our original appropriation for fiscal year 1977 was enacted. The third item, travel for members of the National Market Advisory Board, was incurred as a result of the Securities Acts Amendments of 1975, which mandated establishment of the Board. However, no funds were made available to pay attendant costs, and we were unable to anticipate the travel expense until after Board members had actually filed for reimbursement.

Mr. Chairman, that concludes the portion of my testimony devoted to H.R. 3721. With the Subcommittee's permission, I would like to turn now to the second bill before you today.

H.R. 3722 would authorize the Commission's budgets for the next three fiscal years—fiscal year 1978, 1979, and 1980. It would establish ceilings of \$64 million for fiscal year 1978; \$70 million for fiscal year 1979; and \$75 million for fiscal year 1980. Our estimated budget requirements for those years are tabulated in Exhibit A attached to my statement.

These authorization figures represent our best estimates of the Commission's maximum operating expenses during the next three fiscal years. They do not anticipate any growth in the number of personnel above our current, permanent level of 2,117 positions. The only real growth reflected in these figures is for continuation of our modernization program. The balance of the annual increases is necessary to allow for the effect of inflation, and for anticipated, mandatory pay increases.

Our authorization request encompasses a proposed \$1 million program increase for Automatic Data Processing in each of fiscal year 1978, and fiscal year 1979. As I have stated, the Commission feels that this modernization program is absolutely essential to the continued effective discharge of our responsibilities under the securities laws. We believe it will result in improved service to the public, and ultimately in cost savings as a result of efficiencies in operations.

Once our records handling system has been converted to micro-graphics, the Commission will eliminate backlogs, missing files, and incomplete records; file retrieval time will be reduced from several hours or days to no more than 15 minutes; file storage space will be compacted to 1/40th of today's requirement; manpower will be reduced and staff utility and efficiency will be increased. Further, the dollar savings per year, when the system has been implemented, will be over \$700,000.

By modernizing our ADP systems, the Commission can realize an overall savings and cost avoidance that approaches \$1.0 million on an annual basis, as well as improving staff support and moving into new areas of support and information services which are precluded by current equipment limitations.

Areas of growth and support as well as benefits are more fully detailed in our comprehensive five-year plan.

As you know, there have been tremendous technological advances in the ten years since the Commission first began using computer capability and automation. Since that time, the Commission's management has had a growing concern with the limitations of our equipment and with the ever-increasing demands being placed on an already overburdened and obsolete system. If this concern is not translated into support, however, problems will only multiply and delays in paper flow will increase.

We have monitored our initial efforts carefully, and in creating our five-year plan we have accomplished two important goals. The Commission has been provided with the framework for ADP and records systems which will provide across-the-board support without becoming so inflexible as to be unable to incorporate future new applications, and we have avoided haphazard and "stop-gap" counter-productive solutions.

Mr. Chairman, this completes my prepared statement. I would like to once again thank the Subcommittee for this opportunity to testify, and for scheduling this hearing in a most timely fashion. I would be most pleased to answer any questions you may have.

EXHIBIT A

Securities and Exchange Commission estimated budget requirements for fiscal years 1977-80

Fiscal year:	<i>Estimated requirement</i>
1977 appropriations-----	\$53.00
1977 program supplemental-----	.88
1977 pay increase (Oct. 10, 1976) supplemental-----	2.39
1977 executive pay increase-----	.23
Revised 1977-----	56.50
Estimated program increase (ADP) 1978-----	1.00
Inflationary increase—3½ percent-----	¹ 2.00
Pay increase—Oct. 1, 1977-----	3.00
Estimated—fiscal 1978-----	² 62.50
Estimated program increase—ADP-----	1.00
Inflationary increase—3 percent-----	¹ 2.00
Pay increase—Oct. 1, 1977-----	3.00
Estimate—fiscal 1979-----	² 68.50
Pay increase—Oct. 1, 1979-----	3.00
Inflationary increase—3 percent-----	¹ 2.00
Estimate—fiscal 1980-----	² 73.50

¹ Includes mandatory within-grades increases of about \$500,000 per year.

² Requested authorization ceilings are somewhat higher in order to allow for unanticipated expenses.

Mr. ECKHARDT. Mr. Broyhill?

Mr. BROYHILL. I don't have any questions, Mr. Chairman.

Mr. ECKHARDT. Mr. Metcalfe?

Mr. METCALFE. Thank you, Mr. Chairman.

Chairman Hills, I would like to know whether or not you have made a breakdown on the minorities that are employed, including the women, by the Securities and Exchange Commission at all levels?

Do you have such a breakdown? Is it available now?

Mr. HILLS. We can make that available to you. If I may speak to that subject a minute, I feel very strongly about that myself. We have the first woman division director in the history of the Commission. I believe we had the first black legal assistant in the Chairman's office in the history of the Commission, and we have the first full-time EEO Director in the history of the Commission. Mr. Savage, an experienced person, has come in with a strong mandate from me to do the job in the EEO area that should be done. He created a few months ago an ad hoc committee comprised of leaders from throughout the securities industry to deal with such problems. On that are the chairmen of all the exchanges and the managing partners of all the major investment banking firms. Our charter for that committee is to emphatically come to grips with the fact that there are not enough minorities and there

are not enough women in the securities field in the capital formation process itself.

So the point you raise is one about which I feel deeply. We have historically not done the job in this area we should have done. We have made, however, I think a very major step forward, and if I may, I would have Mr. Savage provide you with the information you are seeking. I would like to make sure it is accurate.

We have recognized the problem and we have moved to deal with it. My own feeling is very deep on this subject and it is that when you go to investment banking firms, when you go to banks, when you go to securities firms, you don't see very many black people and you see precious few women.

It is frustrating to me that the President is having trouble finding experienced securities lawyers who are women or black.

Just recently, we have interviewed a very fine professor from North Carolina, Jim Bauer who is black. He is a commercial lawyer. He was a student of mine the year I taught at the Harvard Law School. I think very well of him. He is not trained in securities law but he is a very competent lawyer. We are bringing him in as an attorney-fellow, and we are going to let him spend 6 months in the General Counsel's office, 6 months in Corporation Finance and 6 months in Enforcement, and then we will have a very senior, capable lawyer of very good judgment who will be a great help to the Commission.

Those are things we are trying to do. We also had a special recruiting program last year in which we made another effort to go through the law schools and find women and blacks, and in particular, to find Chicanos. We have had a very poor record with respect to Spanish-speaking people in the Commission, even in our southern California office and in our Southwestern offices down in Texas. We have had very few people of Spanish background.

Mr. ECKHARDT. Without objection, the record will be kept open for Chairman Hills' reply to your question.

[The following material was received for the record:]

Grade	Total employees			Total white			Total minority			Total female		
	Male	Female	Total	Male	Female	Total	Male	Female	Total	Minority	Nonminority	Total
GS-1	6	2	8	1	1	2	5	2	7	2	2	2
Percent of total	75.0	25.0	100.0	12.5	12.5	25.0	62.5	25.0	87.5	25.0	25.0	25.0
Temporary	1	7	8				1	7	8	7	7	7
Percent of total	12.5	87.5	105.2				12.5	87.5	100	87.5	87.5	87.5
Wage rate	18	23	41	4	3	7	14	2	16	2	3	5
Percent of total	78.3	21.7	100	17.4	13.0	30.4	60.8	8.7	69.6	8.7	13.0	21.7
GS-2	1	12	13		5	5	1	7	8	7	5	12
Percent of total	7.7	92.3	100		38.5	38.5	7.7	53.9	61.5	53.9	38.5	92.3
GS-3	34	59	93	14	25	39	20	34	54	34	25	59
Percent of total	36.6	63.4	100	15.1	26.9	41.9	21.5	36.6	58.1	36.6	26.9	63.4
GS-4	25	97	124	4	50	54	21	49	70	49	50	99
Percent of total	20.2	79.8	100	3.2	40.3	43.5	16.9	39.5	56.5	39.5	40.3	79.8
GS-5	37	147	186	13	94	107	24	55	79	55	94	149
Percent of total	17.7	80.1	100	7.1	50.5	57.5	12.9	29.6	42.5	29.6	50.5	80.1
GS-6	17	125	142	4	78	82	13	47	60	47	78	125
Percent of total	12.1	88.0	100	2.8	54.9	57.8	9.2	33.1	42.3	33.1	54.9	88.0
GS-7	30	81	111	18	50	68	12	31	43	31	50	81
Percent of total	27.0	73.1	100	16.2	45.1	61.3	10.8	27.9	38.7	27.9	45.1	73.1
GS-8	6	22	28	4	13	17	2	9	11	9	13	22
Percent of total	21.4	78.6	100	14.3	46.4	60.7	7.1	32.1	39.3	32.1	46.4	78.6
GS-9	51	18	69	42	13	55	9	5	14	5	13	18
Percent of total	73.9	26.1	100	60.9	18.8	79.7	13.0	7.3	20.3	7.3	18.8	26.1
GS-10	3	4	7	2	3	5	1	1	2	1	3	4
Percent of total	42.9	57.1	100	28.6	42.9	71.4	14.3	14.3	28.6	14.3	42.9	57.1
GS-11	147	40	187	132	31	163	15	9	24	9	31	40
Percent of total	78.6	21.4	100	70.6	16.6	87.2	8.2	4.8	12.8	4.8	16.6	21.4
GS-12	233	43	276	209	34	243	24	9	33	9	34	43
Percent of total	84.4	15.6	100	75.7	12.3	88.0	8.7	3.3	12.1	3.3	12.3	15.6
GS-13	324	27	351	309	26	335	15	1	16	1	26	27
Percent of total	92.3	7.7	100	88.0	7.4	95.4	4.3	.3	4.6	.3	7.4	7.7
GS-14	184	10	194	177	9	188	5	1	6	1	9	10
Percent of total	94.9	5.2	100	92.3	4.6	96.9	2.6	.5	3.1	.5	4.6	5.2
GS-15	108	4	112	104	4	108	4		4		4	4
Percent of total	96.4	3.6	100	92.9	3.6	96.4	3.6		3.6		3.6	3.6
GS-16	30	1	31	30	1	31	3		3		3	3
Percent of total	76.8	3.2	100	96.8	3.2	100.0	8		8		8	8
GS-17	7	1	8	7	1	8	7		7		7	7
Percent of total	87.5	12.5	100	87.5	12.5	100.0	5		5		5	5
GS-18	5	5	10	5	5	10	5		5		5	5
Percent of total	100.0	100.0	100	100.0	100.0	100.0	100.0		100.0		100.0	100.0
Total	1,267	709	1,976	1,081	440	1,521	186	269	455	269	440	709
Percent of total	64.1	35.9	100	54.7	22.3	77.1	9.4	13.6	23.0	13.6	22.3	35.9

Grade	Total employees			Total white			Total minority			Total female		
	Male	Female	Total	Male	Female	Total	Male	Female	Total	Minority	Nonminority	Total
Attorney	552	73	625	525	63	588	27	10	37	10	63	73
Percent of total	87.3	11.7	100	84.0	10.1	94.1	4.3	1.6	5.9	1.6	10.1	11.7
Analyst	92	15	107	90	12	102	4.2	3	5.5	1.3	12	15
Percent of total	86.8	14.0	100	84.9	11.2	95.3	1.9	2.8	4.7	2.8	11.2	14.0
Acc	113	3	116	106	3	109	7		7		3	3
Percent of total	97.4	2.6	100	91.4	2.6	94.1	6.0		6.0		2.6	2.6
Exam/inv	198	8	206	190	8	198	8		8		8	8
Percent of total	96.1	3.9	100	92.2	3.9	96.1	3.9		3.9		3.9	3.9
Technical	35	19	54	25	11	36	10	8	18	8	11	19
Percent of total	64.8	35.2	100	46.3	20.4	66.7	18.5	14.8	33.3	14.8	20.4	35.2
Cler. 1 Sr.	141	530	671	55	303	358	86	227	313	303	303	530
Percent of total	21.0	79.0	100	8.2	45.2	53.4	12.8	33.8	46.7	33.8	45.2	79.0
Administrative	66	36	102	50	26	76	16	10	26	10	26	36
Percent of total	64.7	35.3	100	49.0	25.5	74.5	15.7	9.8	25.5	9.8	25.5	35.3
Miscellaneous	47	17	66	34	9	43	15	8	23	8	9	17
Percent of total	74.2	25.8	100	51.5	13.6	65.2	22.7	12.1	34.9	12.1	13.6	25.8
No title	4	3	7	2	2	4	2	1	3	1	1	3
Percent of total	66.7	42.9	100	33.3	33.3	66.7	33.3	14.3	42.9	14.3	33.3	42.9
Service	17	5	22	4	3	7	13	2	15	2	3	5
Percent of total	77.3	22.7	100	18.2	13.6	31.8	59.1	9.1	68.2	9.1	13.6	22.7
Total	1,267	709	1,976	1,081	440	1,521	186	269	455	269	440	709
Percent of total	64.1	35.9	100	54.7	22.3	77.1	9.4	13.6	23.0	13.6	22.3	35.9

Minorities

Grade	Black			Spanish speaking			Native American			Orientals			Authorized ceiling
	Male	Female	Total	Male	Female	Total	Male	Female	Total	Male	Female	Total	
GS-1	5	2	7										
Percent of Total	62.5	25.0	87.5										
Temporary	1	6	7										
Percent of Total	12.5	75.0	87.5										
Wage rate	14	2	16										
Percent of Total	60.8	8.7	69.6										
GS-2	1	7	8										
Percent of Total	7.7	53.7	61.5										
GS-3	20	33	53										
Percent of Total	21.5	35.5	57.1										
GS-4	18	48	66										
Percent of Total	14.5	38.7	53.2										
GS-5	22	50	72										
Percent of Total	11.8	26.9	38.7										
GS-6	13	44	57										
Percent of Total	9.2	31.1	40.1										
GS-7	11	30	41										
Percent of Total	9.9	27.0	36.9										
GS-8	2	7	9										
Percent of Total	7.1	25.0	32.1										
GS-9	9	5	14										
Percent of Total	13.0	7.3	20.3										
GS-10	1	1	2										
Percent of Total	14.3	14.3	28.6										
GS-11	11	9	20										
Percent of Total	5.9	4.8	10.7										
GS-12	19	9	28										
Percent of Total	6.9	3.3	10.1										
GS-13	20	3	23										
Percent of Total	2.9	.3	3.1										
GS-14	1	5	6										
Percent of Total	1.6	.5	2.1										
GS-15	2	3	5										
Percent of Total	2.7	2.7	5.4										
GS-16													
Percent of Total													
GS-17													
Percent of Total													
GS-18													
Percent of Total													
Total	16.3	25.5	41.8	11	7	18	2	2	4	10	5	15	
Percent of Total	8.3	12.9	21.1	0.6	0.4	0.9	0.1	0.1	0.2	0.5	0.3	0.8	

Mr. METCALFE. Thank you very much for your very encouraging statement on the program you are pursuing.

Mr. HILLS. Thank you.

Mr. ECKHARDT. Mr. Chairman, you have about 200 people in the Enforcement Division.

Mr. HILLS. Sometimes it looks like we have 2,000, Mr. Chairman. That is roughly correct, yes.

Mr. ECKHARDT. About how many of these are lawyers?

Mr. HILLS. I believe it is slightly over half.

Mr. SPORKIN. We have right now only about 180 staff members, including approximately 105 lawyers.

Mr. ECKHARDT. Do you have economists?

Mr. SPORKIN. We have financial analysts and accountants.

Mr. HILLS. Mr. Chairman, you are taking a position I am very fond of. It is my hope that before long we will have a senior economist in the capacity of the dissertation level or above to be with each division. Mr. Zecher, of the Office of Economic Research, is developing that capacity. He was chairman of the Department of Economics at Tulane. His present deputy was the chief economist of the Federal Reserve Board in St. Louis.

We are hiring four economic fellows who are to come into the Commission at a very high level. We are trying to create a capacity to put economic analysis at the hands of each one of the divisions, and I believe that the principal benefit of our modernization program would be to permit us to have random access to our files, to give an early warning system to the enforcement division and to develop the software programs that enforcement can use so as to most efficiently employ their resources.

That is precisely what we are working on now.

Mr. ECKHARDT. How many of the 180 are economists presently?

Mr. HILLS. There are only financial analysts in the division at present. Of course the Office of Economic Research is available to them.

Mr. ECKHARDT. How many financial analysts?

Mr. SPORKIN. We have approximately 15 to 20 financial analysts.

Mr. ECKHARDT. What is their scholastic or training background? Are they professionals?

Mr. SPORKIN. Normally, we try to obtain the highest caliber we can. They will normally have a bachelor's degree at the minimum and usually will have a good amount of work experience, some with master's degrees. But we would usually like to have some experience in the marketplace, either having worked with a self-regulatory body or a member firm so they will have some background.

Mr. ECKHARDT. Are there any accountants that are not so listed as financial?

Mr. SPORKIN. Sure.

Mr. ECKHARDT. How many accountants?

Mr. SPORKIN. We have approximately 12 CPA's.

Mr. HILLS. How many do we have in the regions, Stan?

Mr. SPORKIN. Certified public accountants?

Mr. HILLS. Yes.

Mr. SPORKIN. In the regions I would say there might be another 10.

Mr. ECKHARDT. Are you including in the 180 regions or not?

Mr. SPORKIN. No, no. Absolutely not.

Mr. ECKHARDT. I am just talking now about your officers here.

Mr. SPORKIN. That is correct.

Mr. ECKHARDT. Twelve CPA's?

Mr. SPORKIN. Yes.

Mr. ECKHARDT. And some others at a lesser level of training.

Mr. SPORKIN. We have a number of investigators who have accounting experience and we would have about 7 or 8 of those in the home office.

Mr. HILLS. We have precisely 10 more accountants in the field.

Mr. ECKHARDT. Then how many other persons of generally professional competence or are there any others?

Mr. SPORKIN. Well, we are trying to develop a paralegal program right now and we are at an infancy stage there. Those are people who do routine legal work but are not lawyers. So you get more work at less cost from our attorneys.

Mr. ECKHARDT. How many of them?

Mr. SPORKIN. Right now we have two or three in the division and we are trying to obtain some more. We also have an administrative assistant who is not included in any of those figures whom I would consider to be a professional who, in effect, is concerned with the entire management of the division, from budget, typewriters, clerical, and things of that sort.

Mr. HILLS. I have had formal discussions over the past 6 or 7 months with a number of the larger investment banking houses. The Commission very much needs to have a better understanding of the trading markets. We are not traders. The trouble is a good trader is making a couple hundred thousand dollars a year and it is hard to get a person that really understands the problems of the trading market.

So I am hopeful that our general counsel will permit us to take on someone who has confidential obligations who would come and be a consultant for us for a period of about 6 months at a time, maybe a year at a time, and would be in the enforcement division or market regulation. While such a person might have some conflicts of interest as to some aspects of our work, we could use him to help our people understand what is happening.

I would hope to develop that capacity both in New York and in Washington. Trading technique is obviously an abstruse specialty and sometimes one can spend hours looking at it and not knowing what they are seeing.

So we are trying hard to develop these other skills to which you are referring.

Mr. ECKHARDT. As I calculate rapidly, then, you have approximately 82 percent of your personnel at some type of professional or just below professional level, and about 18 percent would be, I assume, clerical, doing more or less routine work.

Mr. SPORKIN. Those are our estimates.

Mr. ECKHARDT. I understand but I am just trying to get a general figure here. I would say about 80 percent are professional and maybe paraprofessional, if you can put it that way, and about 20 percent are more or less routine clerical.

Mr. HILLS. I think the chairman is quite close. We had that personal services data sheet in the record, do we not?

Mr. HAYNES. Yes; in the budget.

Mr. ECKHARDT. I can understand, Mr. Chairman, that by increasing the efficiency by better routines that you can do with a relatively smaller force, and I also understand what you say that where you have developed more efficiency in other areas of your operation it may give you some room to expand with respect to enforcement.

But the thing that still concerns me somewhat is that amongst professionals, these more or less mechanical means of achieving greater efficiency are not so terribly meaningful. I was always somewhat concerned about Mr. Kleindienst's ideas of having lawyers make an accounting of every 15-minute segment of their work. Of course, that is utterly impossible.

Mr. HILLS. It is even when you bill the time.

Mr. ECKHARDT. That is right. And when you don't bill it, I imagine it's even harder and perhaps more fictional.

Mr. HILLS. We do not do that.

Mr. ECKHARDT. However, I do not know. There is also a large inclination to make some of the bill times up perhaps. But it does seem to me there is an enormous problem here of doing the kind of job that you envision in your budget justifications, particularly in the enforcement division with a staff which is now, even under your normal projected level—

Mr. HILLS. I can only repeat what I feel very strongly about, and that is we should not add people until we know how to use them, and until we have the capacity to use them well, until we have the capacity to train them well. The most glaring deficiency, frankly, I saw at the Commission when I got there was the regional offices. There wasn't a single decent library in any of the regional offices, with perhaps the exception of New York. Just making those tools available to a lawyer so he doesn't have to spend an hour or two going back and forth to a library increases the capacity of a regional office by 20 to 30 percent.

We had some unhappiness in the regions, not with our people but with their capacity to work. We had little idea, at least contemporaneously, of what was going on in the regions. So we began with Stan's people what we call a Notice of Inquiry, and that means every week we get a computer run of every inquiry that was started any place in the country. We also now meet frequently with regional people. In fact, Stan and I are going to Atlanta tomorrow to meet with all of the regional administrators. We meet outside of Washington twice a year and once in Washington with the regional administrators to see how we can strengthen the role of the regional offices.

Again, the most obvious fact was that they could not be terribly helpful to us in many areas because they did not have access to our records. It took too long to get records back and forth.

So we are developing a remote display by cathode ray tube. In 1978 all of our files will be available to them in their regions by having these remote cathode ray tubes, which will have printout capacities; thereby, our files will be their files.

Again, it is not just the enforcement division; it is the enforcement division aided by the General Counsel's office which handles appeals in enforcement matters. It means making that office better capable of handling the work. It meant a special recruiting effort for senior attorneys. It meant a special training program for lawyers so they can become better senior trial lawyers.

It is amazing how much you can do with even one person. We attracted a very competent trial lawyer from Oakland who had 6 months on his hands and he came in and spent 6 months with Stan sitting in the middle of the enforcement division, helping Stan, giving Stan advice of how big cases should be tried and how he could better help train his younger people. And I think probably one of the most dramatic things that the Division has been able to develop is this training program with Columbia University, to give our people this added professionalism. The multiplier effect is terribly important.

I have no way of quantifying the impact of having an outside audit committee on every listed company's board. But I can tell you, going back to 1970 when, by accident, I became embroiled in a large corporation that lost \$90 million before I was able to read the budget, that the lack of an independent quality in the board in that Fortune 500 company, in my judgment, was the reason I lost the money. It wasn't corruption, it wasn't stealing. It was just plain foolishness. At that time use of an outside audit committee composed of independent directors, was rare. Now—the majority of listed companies have outside audit committee. Use of such committee is going to have a substantial beneficial effect on our work. We tell the outside auditors that they have the responsibility, when they see something questionable, and they have a legal liability, to bring that matter to the attention of somebody who has the capacity to deal with it.

If you don't have an audit committee with outside directors, you have no place to go. The auditor's only alternative is to resign the account if something looks funny. All the economic incentives, obviously, are directed toward keeping the account.

So those kinds of things, the multiplier effect, if you will, is terribly important. The multiplier effect can be seen in the 22 audit committee reports now mandated by the Federal court to look in to questionable payments. Is it 22, Stan?

Mr. SPORKIN. There are about 25 companies.

Mr. HILLS. Yes; and you take those 25 independent audit committees mandated by the Federal courts studying those corporations, you have more money being spent than our entire annual budget during the next year just from that effort by independent, competent lawyers that have done this.

That is how this Commission can enforce the securities laws. But I must candidly say to you I cannot really answer the question as to whether we should have 10 or 20 more lawyers. We have to create our priorities. My successor may be back here next year saying, we have finished our management program; we have got our computer system in reasonably good shape; we have taken 25 people out of the office of records and put them in enforcement; we have taken 30 people out of other places and put them in the General Counsel's and we still need 50 more people.

But I cannot tell you that is what we need right now.

Mr. ECKHARDT. Your agency, I think, enjoys the highest reputation among lawyers who have practiced before, it, from objective reports that I have seen, than any Federal agency. And I suspect that one of the reasons for that is that you deal with relative equals. The persons whom you regulate are articulate and are themselves well represented, and are of somewhat equal force in the market place. And I think that I just hope that you continue to enjoy that reputation.

The only thing that worries me somewhat is that, of course, there could be a divide, at which point the SEC, with the growing responsibility as the national market place develops, might be simply overwhelmed, and it might turn out at some time in the future that matters of significance should have been identified, though perhaps they did not involve intentional wrongdoing—after all, you are dealing with an area in which the question of honorable and desirable conduct can not be precisely defined.

And I feel that the enforcement division is a very key part of this operation. I merely suggest this, not as a criticism, but as an added caveat.

Mr. HILLS. I appreciate, accept, and agree. No one has more respect than I for the capacity of the enforcement division. But I think the chairman should understand that all of the resources of the Commission, in one way or another, are devoted to enforcement-type activities.

I will give you just one example and one request.

We have a very large division of corporation finance. Almost all of their time historically has been spent reviewing documents before they are filed to tell and advise people as to whether the document is sufficient.

My own judgment is that that is a broad waste of time and that we should make those forms simpler, more obvious, and not spent as much time with that, and those people with the capacity that our computer system and micrographics will give them should be spending their time reviewing industries. They should be looking at comparable statistics. They should have a 5-year program of going through the shipping industry, the automotive industry, the insurance industry, and they should be doing analysis which would be, then, capable of being used by the enforcement division.

It would not only make it a more interesting job, but be far more productive to create the kind of early warning system that the chairman speaks of. And if we do not equip the Commission to do that, we will be, indeed, overwhelmed because there is no way that you could quadruple the size of the Commission. We cannot, as an original proposition, investigate 11,000 companies that are listed and try to find out which of them are committing faults. We have to have better access to information and better surveillance standards.

We do have problems, Mr. Chairman. Probably the single, greatest problem affecting the efficiency of the Enforcement Division is space. We have gone through the battle of Buzzard's Point and we are going through the battle of GSA.

We are frustrated by a form of bureaucracy that I think is totally unacceptable and wasteful. The Commission needs about 40,000 square feet. Anyone who has seen the halls of the Enforcement Division or the halls of the General Counsel knows that we are in an incredible crunch. We have senior investigators and attorneys sharing office space. We have no conference rooms. We don't have rooms in which to put files. We have just shipped 350 files out of the Commission to make a little more room available.

There is space directly across the street in a building that could be leased for 2, 3, or 4 years, and there is some land behind the Commission that is taken up by parking lots and is an eyesore. And this Congress and the GSA and the Government can figure out a way to buy that land, and build additional space for us and to give us space for a

couple of years across the street while this is being done. This would save money in the long run because we are not efficient in our present overcrowded state, and it's costing us money and is frustrating. It not only frustrates the Enforcement Division in terms of just finding things and moving around, but it is obviously discouraging to people who come to the Commission and find themselves in such an incredibly obsolete working environment.

We have a turnover far greater than we ought to have, which we would not have if we could make better living arrangements available for the Commission.

The number one, first priority for this Commission is to get more space. I have fought for it for one and one-half years with a total lack of success. I have suggested to people who have been named as possible successors to me they ought not to take the job unless the President looks them in the eye and says he will get the space for them. It is critical.

Mr. ECKHARDT. I understand that problem. Do I understand correctly that you have certain limitations with respect to getting space across the streets because of some constraints such as maximum rental charge?

Mr. HILLS. GSA has a maximum rental charge which makes a lot of sense in terms of administering all of government. But it would be sensible in this case to waive that specification for 3 or 4 years to meet an emergency that came about because of the foolishness of trying to put this agency somewhere else.

To allow this agency to spend for 3 or 4 years a dollar per foot above the usual GSA limit strikes me as not destroying the bargaining power of the Federal Government in other leases.

Mr. ECKHARDT. That limitation is not statutory. It is administrative, is it not?

Mr. HILLS. It is totally administrative. To do the job of building additional space for the building, you would need about 100,000 square feet more for the Agency. That would allow us to consolidate all of our efforts in the building. I do think that would take a one-time statutory initiative to permit us to do that and to let the Government negotiate space for us at a fair price. But we could alleviate our problem in 60 days administratively.

Mr. ECKHARDT. Mr. Broyhill, do you have any questions?

Mr. BROYHILL. No questions.

Mr. ECKHARDT. Mr. Opper, do you have any questions?

Mr. OPPER. Yes, I have a question on the budget for the Division on Investment Management.

According to the budget request, the Commission's goal is for 2-year inspection cycles for investment companies and investment advisers. The budget does not increase the size of the investment management division staff, nor of the regional offices which most often conduct these inspections.

Presently, inspections of investment companies are carried out once every 5 years. It is anticipated that in 1978, they will be performed every 5.1 years. In 1978, investment advisers will be inspected once every 9.4 years.

How does the Commission anticipate reaching the goal of an inspection once every 2 years, based upon no increase in staff?

Mr. HILLS. Let me answer generally, and then I will have Miss Jones, who is Director of the Division, perhaps respond.

The regional administrators and others in the Commission have questioned in the past, and I think Miss Jones more than anybody else has questioned, the need to investigate some people who fall in these categories. Some are so small and simple in their operations that a simple sworn statement mailed in as to the extent of their activities can suffice. Also, we believe that we can organize the investigations and inspections, if you will, in a more rational fashion, and thus speed them up.

I am not sure that we can accomplish our goal here. I fully share your concern. Again, we must equip our regions to be more useful in this area, and we are hopefully making that step. And Ann, perhaps you can answer that better.

Ms. JONES. With regard to investment advisers, specifically, we are working on a questionnaire which we hope to have cleared through GAO to mail to advisers, which will give us an awful lot more information than we now have in-house. This was designed as a first step which will aim us at the kinds of questions we should be looking for in inspections and hopefully will make them more efficient.

With regard to working with the regions, we have in the last year, and have continued to do so this year, conducted several regional office seminars where we have sent some of our top people out in an attempt, again, to make the inspectors in the field more able to do an efficient job.

Unfortunately, we often do have to take the people off the sort of routine inspection to send them out on for-cause inspections. But with that in mind, we have also devoted some of our home office staff to the inspection function, which is something we had not done before but we had budgeted for specifically. So some of the people who work most intimately with inspections are available to assist the regional offices in big inspections. In fact, in the last 3 months, we have sent three different people for 3-week periods to California and Texas to do some of the larger inspections.

When will we get to a 2-year cycle? I don't know. It is very difficult to predict, especially—not so much because of daily problems but because of the for-cause inspections that take you away from a systematic approach.

Mr. HILLS. Mr. Opper, I might add one word.

I have some of Miss Jones's frustration about this area. All I can say is we have to depend upon our staff to come up with ways in which we can do things. What more can we do?

We do have resources. If a man came to me this afternoon and said, "All right, I had an idea and I need two people to do something," we would find money for that. I had a surplus budget in my office, in the Chairman's office. The money is there. For anyone in a position to manage any business enterprise or any organization the first rule is don't ever tell somebody you can't do it because you don't have the money. I regard that as an impossible ducking of your responsibility. I have not had to say it. Sometimes I say it is not a good idea, let's not do it. But I have not had to say, we don't have the money to do something.

Mr. ECKHARDT. Aren't there occasions, though, when you say we have to select between priorities and isn't that somewhat saying the same thing?

Mr. HILLS. I don't think so, Mr. Chairman, because I have not had to do that with respect to a matter. I have sometimes argued, sometimes successfully and sometimes I have been outvoted, that we need not investigate something because some other agency is doing it already and we are just coming in later on.

When that happens sometimes, it is not because I feel we can't afford it. It is because I see no particular benefit to the investor in us adding our weight to it. I argue that quite often. But the majority of the time the Enforcement Division talks me out of it. Once in a while my fellow commissioners talk me out of it. But that is not choosing between priorities.

The priorities we are choosing from are in the modernization program. Once in a while we may consider that we have an awful lot of money invested in a particular enforcement matter. We may have spent a lot of money on it. And we may determine that we'd better settle the case because we don't have the resources in the regional office to try it immediately.

But the way to deal with that is to find more trained people and you don't do that in an afternoon. It's not solved just by a budget increase; it's solved by long range planning to get more people with that skill.

In the 17 months I have been in the Commission I have not seen something come before me and had to say no, we won't do this because we don't have the money; we have to do this instead. We have simply not had to do that.

Where I have had to say we cannot do that, it has been because it is not right for doing.

For example, just a few months ago the Investment Management Division said that they proposed to us an advisory committee with respect to investment advisers. And I was looking at a bank study that was overdue to the Senate, and I said, no, let's put that off for 6 months because we don't have the supervisory personnel in investment management right now who can devote the kind of time to this study that a competent group of outside advisors would want. So that was a case of a priority item put off because it could be managed better at a later date.

Not so long ago in the Division of Market Regulation we said to the industry, we are not ready to approve puts. This was last fall. We caused a great deal of anguish because people said we have a program for a pilot project on puts and we want puts to be traded. But we said, I am sorry, we are going to have to wait several months on that. We waited 6 months because we had so much going on in market regulation, that we were not capable of doing it earlier.

And I must say to you in that case that even if we had 400 more people at work at the Commission, the four of us Commissioners weren't capable of absorbing the question of puts at that time. I was not capable of making a thoughtful decision as to whether put trading should be permitted then.

So we have those kinds of priorities put upon us by the 1975 amendments, and we are trying to work our way through it but it is hard.

Mr. ECKHARDT. How many economists do you have in the whole operation, not just Enforcement?

Mr. HILLS. Approximately 30. We have 27 in the Office of Economic Research, and we have a few others scattered around. We also, Mr. Chairman, have a number of very substantial subcontracts with uni-

versities that are doing work for the Office of Economic Research in our attempt to get a conceptual framework for the market percent in option training and doing a number of studies.

So we have greatly multiplied the economic capacity of the Commission in that way. We have signed a study agreement with the Department of Commerce quite recently which I am really quite pleased with. It will involve about \$400,000 from the Department of Commerce that will help us monitor the impact of the regulations we have with respect to capital and we are creating econometric models for doing this kind of monitoring, which would hopefully be usable in many other areas.

So we have had a very large capacity which we are trying to define, as I say.

Mr. ECKHARDT. I would like to explore a little bit these persons in Enforcement. Maybe Mr. Sporkin can answer on this.

As I was calculating here, there are about 18 percent other than professional—who does the typing of the professionals? Do you have some kind of a pool or something?

Assume a firm of 105 lawyers. A law firm of that size would have an enormous supporting staff for that group, certainly more than 32.

How do you handle that?

Mr. HILLS. If I may, Stan feels very strongly about this and I feel just as strongly.

We do not have sufficient support. Again, 17 months ago, we had awful equipment, we had unmatched typewriters, we had no Lexitron 7 months ago.

How many do we have now?

Mr. SPORKIN. We now have eight.

Mr. HILLS. There is a device that costs, what? \$600 a month?

Mr. HAYNES. Yes.

Mr. HILLS. There is \$7,200 times 8. A Lexitron can do an enormous amount of work in the Enforcement Division. We do not have enough sophisticated dictating equipment, we do not have all kinds of things. We don't have good file cabinets. We don't have enough room, of course. But it is this kind of modernization that we need support on.

I have no doubt that we should be developing more parapprofessionals, more secretaries, more support for our people so they can spend their time working to their capacity.

I can tell you we are lacking in this area.

Mr. ECKHARDT. I don't see how you do it. You don't borrow secretaries from other departments or have some kind of a pool?

A highly trained lawyer, particularly one who has also taken special training in the security field, who types his own briefs in rough draft and then lets somebody else copy them, is a pretty high paid secretary.

Mr. HILLS. The General Counsel some time ago made a rough survey and found that in his office lawyers were spending a significant percentage of their time typing, which is monstrous. And again, we used Lexitrons and other devices to speed that up.

We haven't done enough of this modernization. In fact, we are still doing it, as you can see from our supplemental budget from our request. We have put about as much new equipment and people in as we can in the period we have been there. I believe it will continue to be increased. There is no lack of budget right now to get secretaries and more support. There is a considerable lack of space.

Mr. ECKHARDT. If you had a law firm of 105 lawyers and you had a supporting staff of one secretary per lawyer, and a number of file clerks, which I suppose a large law firm would ordinarily have, you would then have 105 man-days of legal activity. But if you have the situation you have, you don't have 105 lawyers, in terms of 105 lawyer-days, do you?

Mr. HILLS. That is correct.

Mr. SPORKIN. You have put your finger on quite a serious problem. As the chairman mentioned, the key problem right now is adequate space. Obviously, I believe we are going to need more people.

Mr. ECKHARDT. Some are in the basement, aren't they?

Mr. SPORKIN. Some are in the basement. Last Monday morning I came in and I have an old couch I brought in and somebody was resting there, and I said, what are you doing? And he said, well, we worked all night long and we had three or four people working all night long, and my heart went out for them.

We have always lived under a tradition whatever the work is we're going to get it done. No matter how many people you give us we're going to get it done whether it means we're going to have to get the outside people to do it or if we do it by having inside people, the job's going to be done as best we can.

Now what we really need, the first priority is we have to get adequate housing. We could not, in good conscience, bring in 50, 60, or 100 more people in the quarters we have. First of all, they wouldn't stay. We are trying to attract very competent people. We are able to do it. For example, we have one senior trial lawyer who happened to run his own firm here in town. He got fed up with it. I talked him into coming with the Commission. I am now in the process of probably convincing two or three other people just like that. They are fed up with private practice, even though they are making three or four times as much as they would in the Government. They have seen what we can do and they like the idea. And I think we are going to be able to attract those people.

The problem that we are going to have is that if we do attract those people, if we don't have an office to give them, if we don't have a secretary to give them, if we don't have the equipment that the chairman mentioned, it is going to be very difficult to keep them.

And I think that is the real problem. But I think the first priority, and I tell you, it is going to be a crisis, if we do not have a place where we can give every professional his own office and appropriate secretarial help. But if a lawyer doesn't have his own office where he can think, where he can write, without having somebody else on the telephone that's going to impede his productivity, he has to be able to concentrate. And that is really the difficulty right now.

Mr. ECKHARDT. I happen to be one who believes that a person in a profession should not be occupied in all of his working hours in definable work. That is, conferring with clients, reading books, dictating.

I think he ought to have some time to think.

Mr. SPORKIN. We don't have that capacity.

Mr. ECKHARDT. I think that if there is not that leeway with respect to those in governmental practice, and there is that leeway for imagination and intuitiveness among those who may have, to a certain extent, an antagonistic position to government, they are going to win out.

I don't know what your view of that is.

Mr. SPORKIN. I think that is the point of giving someone an office, so that he can have a place where he can think for a few hours.

Mr. ECKHARDT. You have apparently a normal staff of around 200, as I understand it.

Mr. SPORKIN. We have never really reached that number. That is what we are projecting. But you have to realize it is the same thing. You get it on Monday and then on Tuesday the President puts a freeze on. You get it Monday and the Congress says, absorb your pay raises or absorb something else.

So we have never really been up to 200 people onboard.

Mr. ECKHARDT. What have been your numbers?

Mr. SPORKIN. Onboard we haven't had more than 180 at any one time.

Is that correct, Larry?

Mr. HAYNES. Yes.

Mr. ECKHARDT. Is that enough?

Mr. HILLS. It is not enough. It is not a budgetary problem that is stopping us. It is the turnover problem, the space problem, and equipment problem.

We don't have a centralized file room. We don't have a sufficient secretarial pool.

Mr. ECKHARDT. Now you say it's not a budgetary problem now. Maybe you have other constraints that prevent you from occupying enough people on the job. But we are talking here about an authorization that will cover a certain period of time. And I hope we do not necessarily have to envisage the present situation that exists. I hope that we can take into account improvements that will more adequately permit you to do the very enormous job that you have got to do.

Mr. HILLS. My best judgment is, and it is one that I have thought a lot about, that we will have under these budget authorizations capacity to strengthen the Enforcement Division—and let me say we concentrate on enforcement, but believe me, the General Counsel's Office, Market Regulation, and others are all in this together and seeking the same objectives. We all have these constraints. We will be able to make the lawyers function as lawyers full time with this budget. We will develop that support mechanism.

We don't really know what the capacity of the force that Stan now has can be if properly supported and properly housed. Just putting a central filing system in and file clerks, that will efficiently get files back and forth, that will track them so that they know where a case is so that he knows what he has, means that a given lawyer is going to greatly improve is efficiency.

We do not have an efficient system, but we have superb people. We are probably getting 53 man-years just from overtime out of the Enforcement Division, and I wouldn't be surprised if it's more. We work enormous hours.

All I can tell you is that I worked, I thought, as hard as a man should work when I spent time at the White House. But I worked, and everybody around me worked at a higher level at the Commission than we did in the White House.

It is an enormous personal sacrifice for some of these people who stay far longer than Chairmen stay with this agency.

Turnover is a considerable problem. What we lose from turnover can never be made up. Because when Stan may have the same manpower, if he loses three people who have been on the case for some time, it is not just a matter of replacing bodies. Even if they are replaced, he has lost probably another man an a half just in getting the new people up to speed.

Those are the kinds of problems that we have. That is where our priorities lie, I suppose, in trying to become more efficient, lower our turnover, and to make the place work better. And within the time limits, I think our staff, I think Larry and Pete Shipman, who has left, have done an incredible job in 17 months. And if we can maintain the supplemental budget to continue the process and if we can get that space, we can design a superb operation.

It hurts me. We started, the chairman may recall, a law firm of our own some 15 years ago. I was proud of the fact that that was probably the most efficient law firm in the country. It did everything in a most efficient fashion. And it brings tears to your eyes to see how we do things at the Commission. It is not the staff's fault; there is simply not enough organized support.

Mr. ECKHARDT. Ms. Nord, do you have any questions?

Ms. NORD. No questions, Mr. Chairman.

Mr. ECKHARDT. Well, Mr. Hills, we very much appreciate your testimony. We recognize the excellent work that your Commission has done and we thank you very much.

Mr. HILLS. Thank you, sir.

Mr. ECKHARDT. The meeting is adjourned.

[Whereupon, at 11 :50 a.m., the subcommittee adjourned.]

