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Cary: Politics and the Regulatory Agencies

Donald C. Cook
American Electric Power Company, Inc.

Politics and the Regulatory Agencies. By *William L. Cary*. New York: McGraw-Hill. 1967. Pp. 149. $5.95.

I. The Book

Professor Cary's *Politics and the Regulatory Agencies* deals with the pressures upon the agencies[1] exerted by the White House and the Congress. It is a curious work. Although the book is in good part autobiography, it is well-nigh barren of any hint of the intense personal feelings that must have been generated in Professor Cary's all-too-short tour of duty as Chairman of the Securities and Exchange Commission (SEC). It is silent on classical issues that have absorbed the SEC in its routine functions as well as its major policy work. Yet the SEC plays a major role in the book, and Professor Cary's time at the SEC was one in which some of these issues were in critical ferment. The book reveals a bias with respect to, but does not come to grips with, the perennially baffling question of just where, in an ideal framework of our government, the administrative agencies belong.[2]

1. As will be apparent from this review, I was considerably disappointed at the book's avoidance of the question of just where, in the tripartite system of government, the agencies should belong. Certainly it is not a problem outside the scope of the book's title, if one is to take the word "politics" in any of its grander senses. The agencies have been variously referred to as "administrative" and "independent," as well as "regulatory." Professor Cary's very theme is the "dependence" of the agencies. He is perfectly justified, therefore, in avoiding the adjective "independent." If the choice of "regulatory" was intended to avoid the pro-executive implications of "administrative" the victory is at a considerable expense of meaning. Almost every branch and sub-part of each of the major divisions of our government "regulates."

2. Professor Cary shows succinctly how a strong President and a strong Senator may have equally strong but opposing views. His own view seems to be Keplerian. The agencies have their own orbits but are subject to the gravitational forces of the larger bodies—forces which are more or less strong depending on issues and personalities.

Yet, paradoxically, the place of the administrative agency is in fact the very theme of the book.

Professor Cary has written an excellent testament of an agency chairman of high competence who was able to temper his dedication with coolness, objectivity, and balance. But a reader searching for broadscale meanings in the torrent of human affairs—which both Aristotle and Kafka would have recognized as "politics"—will be disappointed. A reader expecting from a former SEC Chairman deep insights into the agency's exciting work, problems, and people will have to look elsewhere.

Since the remainder of this review will deal mainly with what Professor Cary did not say, the author is owed the courtesy of a summary of what he did say.

Part 1 deals with the White House as a force at work upon the agencies. An agency is subject to the hazards of the quality of the man or men in the White House with whom it must deal. Implicit in this section of the book is a warning that, by and large, an agency chairman does well to be as aloof as possible from White House staff. In part, this is because a jealous Congress may be watching.[3] Professor

The ordering force in this planetary system is not an ideal about the structure of government but the substantive job of the agency. This may be consonant with American history and with our drive toward efficiency. Whether it is an unmixed blessing is another question. To deny the role of accident and power play in the making of our constitutional history would be fatuous. What would the Constitution "be" if John Marshall had never sat on the Supreme Court, if enough votes had been gathered for the impeachment of Andrew Johnson, or if the Roosevelt "courtpacking" plan had succeeded? Yet to deny the abiding power (and need) for permanent constitutional principles is dangerous. While the practical truth is almost always a vector of the moment's force and abiding ideal, the latter should never be the weaker. Despite a large body of precedent in cases and practices, and whether one uses the word "constitution" to denote a specific document or a sense of ideal in government—or even as a description of the mood of the moment—finality in the placement of the agencies in a "constitutional" framework has not been achieved. One might expect a statement that the question is not important, that the answer can only be a temporarily valid one, or that the preference should be for one or the other situs for the agencies. But it is difficult to be content with Professor Cary's statement that President and Congress should use "teamwork." *See* note 5 *infra.*

3. The incident chosen by Professor Cary to illustrate the dangers of yielding to White House pressure occurred in 1955. Sherman Adams, assistant to President Eisenhower, asked the Chairman of the SEC to defer the examination of a key witness in hearings on the Dixon-Yates affair. His reason was that government attorneys, upon whom the President would rely in deciding whether to take a position in the matter, were out of town. The Chairman conveyed the request to the full Commission, which granted the request. Some two years after the incident, in a Senate committee hearing, an important Senator branded the incident as a case of "interference" with the SEC, which, according to the Senator, "is an arm of Congress." From the hearing excerpt quoted by Professor Cary one gathers that the sin, as the Senator saw it, was not so much the "interference" itself but the fact that the request for continuance was sought from the Chairman of the SEC "who would ultimately have to pass upon the decision of the trial examiner" rather than from the trial examiner himself (pp. 13-15).

The Senator's reasoning is a fancy loop which does not make a knot. The significant difference between the President's approaching the agency chairman, rather than a trial examiner, with a thoroughly legitimate request is that to approach the trial

Cary lists the various controls over agencies available to the White House (appointments, preliminary budget clearances, personal contacts)[4] and sets them beside the pressure techniques available to the Congress (reminders that the agencies were created by acts of Congress, open hearings, budgetary approvals, changes or threats of changes in administered laws). He believes that neither the White House nor the Congress should play for the upper hand but that both should operate through "teamwork" in bringing about effective reforms.[5]

Part 2 is an anecdotal recital of the modes of pressure Congressmen exert, or try to exert. While Professor Cary concedes the value of "legislative oversight" (a startling phrase which connotes a "watchdog" activity of Congress), and while he bows to the power of Congress to influence agencies through fully passed changes in the law, he regrets the attempts of congressional committees to influence the work of agencies through "directives" collaterally made in reporting budget awards, pressure exerted in public hearings, or the harassment of requiring from agencies elaborate reports which pre-empt agency time and energy.[6]

Part 3 deals with the problems of a new chairman of an "old-line" agency in revitalizing the agency after years of an unsympathetic administration. (Professor Cary was a Kennedy appointee.) Oddly enough, in a book whose potential force is considerably frustrated by its frequent findings of neat balances of equities, Professor Cary criticizes the "balancing" philosophy of agency appointments—for example, the theory that the commission heading the agency should contain pro-industry as well as pro-consumer men, hold-backers as

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examiner would be a bizarre departure from courtesy and protocol. Of course Professor Cary knows this. He does not, however, say so. Perhaps he saw that the Senator's statement cooked its own goose well enough without the basting of Professor Cary's comment. Or perhaps the failure to make a point of it arises from the particular context of Professor Cary's discussion of the incident, which is not the merits of the case but its illustration of the dangers of embarrassment to an agency chairman from contact with the White House.

4. Personal contacts with the President himself are not among those intended by Professor Cary as White House routes to power over the agencies. This may be true of his regime. At times, however, because of the importance of an issue or because agency people are either personally or officially implicated in inter-agency programs of high priority, the President's voice is heard and must be heeded. In earlier days of its history the SEC was an important reservoir of talent for trouble shooting in many unrelated, as well as related, areas of government. When close contact is had with a President, his power may be great without his needing to exercise it—even if only because agency people sense his mood and his will.

5. To the comments already made in note 2 *supra* should be added that while teamwork between White House and Congress always exists, so does the more or less intense competition for power which takes place through the operation of personality and strategy that express themselves in the teamwork.

6. Here, as elsewhere, Professor Cary's discussion is more valuable as anecdote than as principle. An agency chairman who maintains close contact with the White House might find in it relief from much of this type of harassment.

well as go-aheaders. Important in revitalizing the agency, according to Professor Cary, is to resurvey broadly its tasks, the changes in its regulatory environment, and the legislative tools with which it works, and to exert, for this purpose, pressure for higher budgets and more "super-grades" into which to attract and elevate good professionals. With characteristic fair-mindedness Professor Cary concedes that his own success in revitalization of the SEC through this route was in part luck and fortuitous historical circumstance.

Part 4 is a case history of an agency (the SEC) maneuvering in the tricky currents of Washington to get a bill passed—in this case the extension to larger "unlisted companies" of financial reporting, proxy, insider-trading, and other requirements theretofore applicable only to companies whose securities were listed on exchanges, and a raising of the qualifications of broker-dealers and others in the securities business. Passage of this law, it should be noted, was a significant achievement. For more than two decades, efforts by a succession of SEC chairmen to have such a bill passed had proved fruitless. However, since the currents of Washington, like those of Mark Twain's Mississippi, are subject to unpredictable change, this log of the SEC's success may or may not be a useful how-to-do-it manual for the future.

Part 5 sets forth Professor Cary's unobjectionable conclusions. He believes in smaller commissions. He believes in presidential appointment of agency heads. Finally, while he concedes that the adjective "independent" as applied to the agencies can be only relative, if indeed it is not a total "myth," the myth, he believes, should be preserved.

Professor Cary's book stays well clear of turbulent waters. The remainder of this review will deal with two aspects of that turbulence. One is the broader social context of the problems with which, in some sense or other, all agencies deal. The other is some of the substantive content of the work of one agency with which Professor Cary and I have some familiarity—the SEC.

II. The Storm Outside

If the Constitution were a tool, it would have been discarded a long time ago. It has survived into the present because it is in fact a chest of tools—with new ones heaped on top of old ones and old ones put to uses of which their creators never dreamed.

We tend, in American government, to do the jobs that lie to hand—fairly sure that somehow one of the tools already in the bin will serve; and, if not, that the old bin will always take a new tool. We have done throughout our history what each contemporary ethos has pushed us to do and have managed to find constitutional justification—whether for the affirmation of property rights in human slaves or, through the device of a decree in equity, for a court's taking on the running of a school system or the redistricting of a political unit. Brilliance in constitutional law has consisted of finding out what it can be made to mean rather than what it does mean. There is, in our day, something antique about the notion of a bench or bar dedicated to an a priori philosophy of government and searching for meanings beyond the social and ethical fashions of the day, whether for or against the protection of murderers and dope peddlers or for or against the protection of enterprise and property.

What might be called our constitutional plasticity has had several consequences which are vital to the character of American history. One is a dynamism uninhibited by overly self-conscious formalism. Another is the ease with which government takes on more and more jobs in a time when the social ethic tends to make every man's needs other men's problems. Since government tends to act in this way by collectivities—of people and technique—more and more of our conscience and work become collectivized, in and by government. A final consequence of an extremely flexible constitution is our tendency to ignore it and to be as unaware of it as we are of a comfortable shoe.

The sum of these consequences is an even larger and more troublesome one. It is a susceptibility to historical traps: to reaching forms of tyranny through urges to promulgate goodness; to eroding fundamental safeguards by constitutional fluidity; and to a proneness to pass on to collective conscience and responsibility more and more of the personal concerns which make up the only kind of man worth having—the concerned man. When, as time goes on, the citizen's hand is removed further and further from the running of things (in large part because so many more things are expected to be done), his participation in the world's work tends to be expressed through his role in selecting the people whose hands move on as his move off.

The historical irony is that the citizen's ability to participate in the selection of the people who administer his affairs goes down as their number and the proliferation of their tasks go up. They are the bureaucracy—the atomized mass of functionaries who persist through political upheavals and whose wall of defense is so much the stronger because it consists of so many small stones piled so high and piled in a circle from which there gets to be less and less chance to escape.

The social revolution through which we are living is perhaps the most profound in our history. It is bigger and more pervasive than many of the great political revolutions and as bloody. To be concerned with where this revolution is taking us, as people and as a society, is perhaps the highest of contemporary intellectual duties.

Holmes sensed this and sensed that this concern should be, in particular, the dedication of lawyers. When he defined law as the self-conscious reaction upon itself of a society seeking to determine its own destiny, he defined the principal mission of the lawyer.[7] No book purporting to deal with a phenomenon as majestic as "politics" or one as baffling as the administrative agency[8] can be immune from criticism in terms of the author's willingness and ability to come to grips with the crises which this revolution brings upon us.

It is from this vantage point that I am somewhat nonplussed in an appraisal of Professor Cary's book. It is a simple, stick-to-knitting treatment of the pressures on an administrative agency resulting from its dual dependence on the White House and on Congress. Professor Cary accepts the hybrid nature of the agency, without ever a groan of agony in attempting to resolve its place in the pattern of constitutional powers. He deals with down-to-earth problems, and his book convinces us that if all men were as fearless, as rigidly honest, and as competent as Professor Cary we would need neither constitutions nor constitutional concerns.

But constitutions were made to provide paths and bridles for the ambitious as well as the humble, for both well- and ill-intentioned men. The urge to goodness, lodged in men to whom good results justify any means, is the prime source of erosion of constitutional patterns, and the prime danger to which concern for the Constitution should be alert. And if this is so, how much more urgent is it to find the templates to mould the course of men not as gifted or as restrained as Chairman Cary?

The Constitution can survive an amazing amount of attack. It does not do as well against indifference. In its way, the Supreme Court has recognized this in the steps it has taken to extend the strictures of the equal-protection clause to state inaction as well as to

7. O. Holmes, *Privilege, Malice and Intent*, in Collected Legal Papers 129 (1920). Holmes' comment was made in the course of his appraisal of the boycott cases of the late nineteenth century. His uneasiness with the "unconscious prejudice" and "half-conscious inclinations" speaking through the mouths of judges led him to stress the importance of the self-conscious, goal-making functions of law and lawyers.

8. Baffling, if for no other reason than that in a government presumably structured by a separation of powers the agency is a sort of total government in miniature. It legislates (through rulemaking). It decides cases (after hearings which, despite the softening of "quasi," are nevertheless highly judicial in character). It prosecutes and defends cases in courts. It investigates. It "polices" in a broad sense and, by virtue of strong investigation and enforcement powers, in a narrow sense as well.

Perhaps most intriguing about the agencies is the possibility that they illustrate our ability to revolutionize concepts of government without ever scratching the Constitution. Born of minds very much influenced by classical thought and eighteenth century rationalism, the Constitution structures government and provides checks and balances in terms of the classical and formal functions of government—executive, legislative, and judicial. What the agencies seem to illustrate is that operating divisions of government need to be structured in terms of specific areas of economic and social concern as well as (or even in preference to) the classical functions.

state action. This kind of thinking tends to make of the Constitution a germinal determinant of our energies and direction. Whatever else one may think of the quagmire of functions taken on by the courts as a result of this step, it is a truly vitalizing one for the Constitution and a revealing one to those who are interested in the philosophy of history. For it illustrates the maxim that social expectations tend to become social goals; that in the outrunning of expectations beyond realities gaps are created; that these tend to be power gaps, which will, sooner or later, be filled.[9]

Because our courts have been so quick to fill the power gaps they have become a principal agency in the extension of conscience into law. So far have they gone in realizing the dreams of men who used to be called "liberals" that they have belied generations of cynicism about law, lawyers, and courts as instruments of the propertied classes. Yet, in that very process, the courts have crossed state and federal lines and wandered freely into other chambers of the government mansion, taking pulses, administering clysters, prescribing diets—in general, assuming functions that once were conceived of as legislative or executive. So far, goodness has been the spur and elevation the result. But I would be far from sanguine about the future if I did not feel that the expanded role now being played by the courts is only temporary—that we will, sooner or later, see a rearrangement of power which revests more of it with those branches of government more amenable than the courts to the will of an informed electorate.

III. Challenges Inside

Part of the history of every agency is the way in which it responds to the power gaps. It can default by failing to recognize and to fill some; it can fault by rushing in too fast to fill others. Perhaps one of the prime values of Professor Cary's book is his recital of instances of the brave agency fights, of the agonies, the victories, half-victories, and defeats in the never-ending tide of battles. He has modestly told the story of an important victory of the SEC (the amendments to the Securities Act of 1934) in the form of a "for instance" in the strategy of relations with the Congress. Thus, the recent more extensive press coverage of the SEC, larger budgets, and larger staffs seem to augur well. But a fuller appraisal of the SEC's present position and prob-

9. The idea that social expectations create political power gaps is, I believe, a central one. A pervading urge in us for decades was to open the country to the free flow of men and goods and information essential to national economy. Those were days when the interstate commerce clause was an overriding concern of the Supreme Court. No sooner was this victory sealed than the tidal wave of expectations beginning with our struggle out of the great depression launched us into the era of the individual—wherever he may be and whatever doing—as a national concern. The state lines have been crossed; the march is now across city and township lines, into the classroom and the police precinct house.

able destiny both as a unit in its environment and as a housing for forces within itself requires some understanding of its extraordinary impotence as well as its unique strengths.

The SEC deals with only a very small fraction of the total flow of capital formation. In the capital mass consisting of internal cash generation, private borrowing, inter-business extensions of credit, government financing, and public issues of securities—to name a few—the last named is rather small-fry. And only a portion of the public issues for new capital is of equities, the type of securities in which protection of the investor is, generally, most necessary.

Thus the public offering registration work of the SEC, which absorbs a large part of its budget, screens only a small part of the total capital raised.[10] A large segment of the horror cases in this portion of the SEC's work—the cases which take time and money to handle—are small equity issues. Yet the plain fact is that a moderate drop in the price of American Telephone and Telegraph may cause more loss for more people than would be caused by the utter failure of whole masses of hot and speculative issues which absorb so much of the SEC's attention.

Perhaps the greatest value in the work of the SEC and in its policing of crooks, swindlers, and unscrupulous salesmen is the exemplary and admonitory value. The actual loss caused by downright fraud in securities selling is undoubtedly insignificant compared with such figures as the amount of money spent for tinted water, low-grade farina in high-priced bologna, drugs which do not cure, or cosmetics which do not beautify. But enforcement and improvement of standards of disclosure—including refinements of accounting standards—have spillover effects that reach far beyond the limited scope of the SEC's work. And the very presence of the SEC as a police force, like the presence of the registration requirement for new issues, tends to sanitize the field.

In terms of social impact one of the most significant areas in which the SEC works is regulation of stock exchanges.[11] The minute-

10. For example, of $81.5 billion of capital funds for non-financial businesses (*i.e.*, excluding banks, insurance companies, savings and loan companies, etc.) in 1966, some $63.5 billion were from internal sources—principally retained earnings and depreciation. Of the externally raised $18 billion only about $1.2 billion was from net new stock issues, of which some $160 million was privately placed (and therefore not registered with the SEC). The bulk of externally funded financing consisted of some $15.6 billion of bonds, of which approximately half were privately placed. SEC STATISTICAL BULLETIN (1966). It should be noted further that a considerable part of the securities registration work of the SEC involves "secondary" issues by investors—issues which do not raise new capital for the issuing company but raise cash for the selling stockholders.

11. Largest of these is the New York Stock Exchange. A distant second is the American Stock Exchange, also located in New York. A good deal of the trading in the so-called "regional" exchanges—Midwest, Detroit, San Francisco, for example—is in securities also listed on the New York Stock Exchange. The exchange markets are places as well as institutions. Trading is done on the "floor" by members acting as brokers (*i.e.*, agents) for their customers at the posts of specialists who also trade for

by-minute ebb and flow of stock prices on the exchanges are instantly broadcast throughout the world. Billions of dollars of current value are created and destroyed in these movements. The tone of the economy, of the society itself, is strongly affected by them. They are not only barometers of economic weather—they are weathermakers as well.

Ideal markets are markets which respond rationally to changes in underlying investment values and investment prospects. But markets are never ideal, and are sometimes tragically the reverse. They can overrespond; they can underrespond; they can respond to irrelevancies and be indifferent to the significant. They can also be manipulated. As to manipulation, the law is plain and the SEC is as vigilant as its budget and human capacity will allow. But even if its antimanipulation work were entirely complete and perfectly successful, the effect on the markets might, I suspect, be almost unnoticeable. The inadequacy of the markets is for most part rooted in the stupidity, ignorance, and greed of large numbers of wholly respectable people who trade in it and is in least part due to generic causes in the mechanisms of the market itself.[12]

I have some familiarity with the organization, mechanics, membership, and management of our major exchange—the New York Stock Exchange. It comes close to the miraculous in its efficiency, its levels of honesty, and competence. Its shortcomings are due mostly to the massiveness of the work it must handle and the limitations on even the best of human capacity and private capital in the face of the huge task of maintaining an orderly flow of transactions and prices.

Yet the exchanges are far from perfect. To bring them closer to perfection and to create a temper among public traders which makes possible a more rational flow of prices are tasks which put at a high premium the exercise of a creative and prehensile imagination. In some sense or other the SEC acts as a sheep-dip for securities and securities practices. The historical reason is, of course, the background from which the federal securities legislation stems. In good part, this was a belief (basically well-founded, but perhaps somewhat

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their own account and who are pivots for transactions, supplying stock when demand outreaches supply, taking stock when the reverse is true. While a specialist is a private individual or firm, acting for profit, his capital and courage are important factors in smoothing over jagged price gaps resulting from disparities between supply and demand.

12. A man whose good sense and business experience have taught him to expect nothing for nothing and whose whole background makes the idea of begging abhorrent may turn tail in stock dealings. When he asks for a "hot tip" he is, in effect, begging. He is assuming that someone will part with information which, if it has any value, the informer would wish to guard for himself. If he follows a reliable tip he may be participating in a rig—for the most reliable predictions of what is going to happen in a stock are made by those who plan to give Providence a helping hand. If he follows an unreliable tip he is a fool.

exaggerated) that the chicanery and malpractice preceding the market collapse of 1929 were significant causes of the intensity of the collapse. Whatever one thinks of this assumption, the fact is that from the first of the securities laws (Securities Act of 1933) to the last (the 1964 amendments to the Securities Exchange Act of 1934) the laws have been necessary and their effect beneficial.

But is the sheep-dip role itself wholly apt for the problems of our day—and of days which may soon be upon us? A root phenomenon of our securities markets has been the rapid increase in investable money in the face of a much slower increase in the supply of available investments. Even more dramatic than the long-range effects of this disparity are some of its short-range effects. It is not unusual for a hypothetical Hepatronics, Inc., with little but hope in its financial statements, to come out at twelve, zoom to thirty-six, and equally fast sink to four when detumescence sets in. Market experts will argue interminably about the relative roles of tax law, public stupidity, and stock salesmen's avidity in bringing this about. But underlying all is the fact of limited supply and expanding demand.

The reinvestment of cash flow, so popular among companies (and investors) today and so basic a reason for the relatively slow rate of increase in investment vehicles, is not an unmixed blessing. There was a time not so long ago when some astute commentators looked askance at it as a major means of providing capital for expansion.[13]

The once classical "bond-stock" ratio (based on the notion that the risk taken in stocks should be compensated for by a more liberal yield) has been well-nigh junked. Liberal dividends on stocks have, in fact, become suspect as indicators of poor growth potential. Yet if liberal return (tomorrow if not today) disappears as the ultimate aim of all investment, then nothing but a permanent trip of the securities markets on the upward road can justify much of stock market action.

13. B. GRAHAM & D. DODD, SECURITY ANALYSIS (1934). The authors, committed to the classical notion that the purpose of investment is return, regarded the basic fallacy of defenders of plow-back to be their failure to recognize that, even when it makes good sense for the business, it may not make equal sense for the stockholders. *Id.* at 329.

At times the difficulty is not with plow-back itself but with the way it is interpreted. Let us suppose that, in the midst of a labor negotiation, management realizes that it is going to have to grant at least a 5% increase in wages—or the equivalent. If labor costs are, say, 50% of the company's operating costs, the increase will result in a 2.5% increase in operating expenses before taxes. It may be able to pass some of this on to its customers. But the likelihood is that its suppliers, facing the same squeeze, are going to pass *their* labor cost increases on to the company. The only safe assumption is that the increase will have to be offset by increased efficiency. New machines, new processes, to bring about efficiency will, in all likelihood, be financed out of cash flow, including retained earnings. Thus, to a great extent, yesterday's profits are plowed back just to stand still. Were they therefore really profits? Further, whatever the reason for the plow-back, it may be only minimally successful—or it may even fail. Yet the tendency is indiscriminately to take the accountant's classification of "retained earnings" for granted and to look favorably upon the plow-back of these earnings as a sign of "growth." It may be a sign of desperation.

Whether the markets can or should take this trip is one question. Quite another is whether a market that must continue to give capital gains (as against a reasonable return on investment) may not be a lit fuse in our economy.

The recent years have been a trying time for investors and analysts of what might now be regarded as "the old school." These are people whose philosophy is based on the assumption that, in the long run, the market price of a stock will reflect the course of its value—up or down. Sensitivity to short-term market price fluctuations was always important, but primarily as a basis for advantageous buying or selling, ultimately based on value judgments. Now short-term fluctuation is on the way to being the sole determinant for many people of what to buy or sell. In recent markets, with buoyant prices for "glamor" stocks and lagging prices for proved and established equities, value judgment may not as often have paid off as have flings in high-flyers, regardless of basic values. The long run for which value judgment waits has, to the despair of many, become longer and longer.

All of this is draining out the relevance, for more and more people, of the major aspect of the SEC's work—disclosure designed to permit the making of prudent judgments about underlying values. The SEC cannot be indifferent to this fact. But within the present framework of its jurisdiction it can do very little about it. The roots of the problem are deep, reaching into the mainsprings of human and corporate motivations: they extend into tax policy, monetary and fiscal policy—including the old "new" economics—wars, welfare, and beyond.

Certainly continued and increasing stress on disclosure is needed. But more certainly it must be recognized that the vitalization of the SEC calls for more than merely more people doing more eagerly more of the same work that has been done for a long time. The prehensile imagination must break treadmill circles and move outward. That it must clamor to be heard by those who make tax, fiscal, monetary, and general economic policy is not the end of hope but the beginning of a task.

But even within the circles of the SEC's endless round there are classical problems worth mentioning. One of these is a competition of basic philosophies. While disclosure has traditionally been the keystone of the arch of federal securities legislation and has been the dominating drive of the SEC, there has always existed a countervailing force within the SEC whose first impulse is not to cure with disclosure but to kill by prohibition.

The two approaches—disclosure and prohibition—are interwoven in the fabric of regulation. The relative emphasis on the one or the other stems not only from the framework of legislative authority but also from the character of administrators. The man whose first impulse is to insist on full disclosure and thereafter leave people free to make their own judgments demonstrates by this fact a point of view about the nature of people and the role of government. It is a point of view consonant with a classical belief in the perfectibility of man, in the possibility of self-improvement, and in the efficacy of enlightened self-interest and with the very hope for a democratic process which is not merely ethically desirable but practically effective.[14] The prohibitor's psychology implies, equally strongly, different points of view. It pretends to possess the power to distinguish between what is good and what is bad. It refuses to credit people with either the ability to use information or the hope of learning to use it. The belief is often generated out of sincere desire to prevent harm and promote good. Its fundamental danger is that these impulses expressed in prohibitions can lead to benevolent despotism and leave us open to the danger of a despotism which is less than benevolent.

Administrative discretion is the mortar that holds together the great blocks of legislative structure under which the SEC acts. In the authority to time the clearance of a registration or proxy statement, in the ability to stretch disclosure requirements, by insistence or innuendo, the SEC's staff enjoys tremendous power to hinder or facilitate (depending on its view of the merits of a proposed corporate transaction), even while administering only a disclosure requirement. For this reason the nature of the man who administers the law can be virtually determinative of whether it will work as a disclosure requirement or will be used as an instrument for the imposition of fiat.

Some staff members who have spent years with the SEC tend to be like policemen who have spent years on the force. They develop, often slowly and imperceptibly, a jaundiced view of human nature. They begin to believe that the public can be helped best by denying access to it by "crooks"—a broad term which is sometimes used to include promoters of worthwhile but untested ventures.[15]

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14. Various "blue-sky" laws (state laws regulating securities issues) either expressly grant or are construed to grant power to state administrators to ban issues for reasons related to their investment "quality." These standards have not, by and large, proved effective. Administratively developed tests—such as a three-year record of dividends—are likely to be entirely inadequate in an appraisal of quality but tend to act as substitutes for rational tests of quality. Pet foibles of one kind or another—such as insistence on cumulative voting rights—often screen out high-quality issues. Unleashed judgment operating under a vague and broad standard—such as "sound" capital structure—can give play to prejudice parading as judgment. The alternative to the tolerance so widely used by state administrators with strong prohibitory powers is nit-picking of equally dubious value in the protection of investors. For a general discussion, *see* L. Loss & E. Cowett, Blue Sky Law 67 (1958).

15. I have heard strong defenders of disclosure in securities transactions insist that some very drastic prohibitional steps ought to be taken in the campaign against

From the human point of view one can understand this process. From the social point of view it is an extremely dangerous one. Despite enormous strides made by the SEC in deepening and broadening the role of disclosure in securities transactions, the public still tends to respond to tip, hunch, and rumor—most often to its loss. It may take more than one generation of administrators to make the slow progress which is all one can expect in this field. But it takes only one generation of administrators to kill the hope of progress by losing heart and taking the easy route of fiat against the painful and stumbling route of disclosure.

The premium on keeping this faith alive in staff members is extraordinarily high. Fiat works. Because of that fact it tempts the regulator into further and further uses of it. Yet every step taken in the exercise of fiat is the death of a hope for the only kind of investor protection which is both permanent and valuable: self-protection.

Professor Cary was the spearhead of recent amendments to the Securities Exchange Act of 1934 which resulted in a long overdue extension of disclosure requirements to companies whose securities are not traded on the exchanges. He was an able and dedicated administrator of the disclosure requirements in his work as Chairman of the SEC. Yet in a casual reference to changes which he feels might be needed in the Investment Company Act of 1940 he asks whether, in the regulation of mutual funds, disclosure should not give way to fiat in the remaking of important statutory patterns. He has more than earned the right to his point of view through his experience in regulation. I happen to differ with him in this case. To substitute fiat for disclosure would be a serious blow to progress in self-protection for a segment of the investment public that urgently needs it. However, my cavil with Professor Cary is not so much over this difference in substance but over the casualness of his treatment of a basic and difficult issue.[16]

Another casual reference by Professor Cary is to the question of whether the SEC should retain jurisdiction to administer the Public

cigarettes and whiskey. The closer one reaches to strong feelings the closer one comes to fiat. The real test of a good administrator is the strength of his resolve to pursue the disclosure route in the face of his strong feelings, not his weak ones.

16. Even a sketch of the merits of the SEC's controversy with the mutual fund industry would be far beyond the scope of this review. But it should suffice to note in this connection that the SEC has proposed among other things, a substantial reduction in the present prevailing scale of fund share acquisition costs. It has also proposed banning certain methods of charging acquisition costs known as front-end loading. These questions are sufficiently important as related to a competitive industry acting under extensive and rigidly enforced disclosure requirements to merit some discussion. Similar but more complex issues are raised by the SEC's proposal that a statutory standard of reasonableness be imposed on mutual fund management fees. Even so slender a volume as Professor Cary's book could carry a deeper explanation of his views on these important proposals.

Utility Holding Company Act of 1935. This law, and the SEC's achievements under it, resulted (in a period of less than two decades) in an enormously valuable restructuring of public utility holding company systems, both gas and electric. This achievement, I believe, will stand for a long time as one of the truly great and permanently valuable pieces of the SEC's work. Certainly, nothing else the SEC has done has yet equalled it.

However, the breaking apart of holding company systems was only half of the job envisioned by the Act. Still undone is the equally important task of charting a course for the integration of utility operating companies for the expanding tasks that lie before them—including the achievement of economies of scale and the kind of reliability that can only come from coordination made possible by larger systems under single ownership. While some progress has recently been made in this direction it has been made voluntarily by utility company managements without help from the SEC.

Professor Cary has been quite blunt in his criticisms of the Interstate Commerce Commission (ICC) for its inertness in the face of enormous problems of American railroads. It was the opposition of the ICC to earlier and more vigorous versions of the Transportation Act that helped materially to delay and, in some cases, make virtually impossible integration and financial revival of American rail systems. To Professor Cary's credit it should be observed that he has done no more than suggest that if the integration job is to be done under the Public Utility Holding Company Act someone else should do it—preferably the Federal Power Commission. To the contrary, it might be observed that the speed and excellence of the SEC's job of breaking up nonintegrated utility holding company systems was due in good measure to the fact that it was done by an agency free of ingrained modes of thought and of embroilment with the perennial and nagging tasks of account classification and rate making. The SEC has been jurisdictionally aggressive in other areas. It would seem rather odd if it were to turn its back on the area in which it did its greatest work and established an enduring reputation; indeed it would be rather sad if it no longer felt equal to the task. But it would be even worse if it kept the power but failed to exercise it.

IV. Conclusion

Just as no man can write a book which does not, in some way, reflect his basic drives and character so too can no man write a review. From this book emerges the image of a man of extraordinary integrity and courage who hungered for and achieved a good measure of effectiveness and independence in his job as Chairman of the SEC. But his book is, perhaps, still too close to that era of his life to enable him to separate fully those aspects of it which exemplify his particular bent from those which exemplify permanent principles and mainstream meanings.

Donald C. Cook,
President,
American Electric Power Company, Inc.;
former Chairman,
Securities and Exchange Commission