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FORMAL WRITTEN TESTIMONY OF ROEL C. CAMPOS, ESQ.

DELIVERED BEFORE THE COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM, U.S. HOUSE OF REPRESENTATIVES

"THE FUTURE OF CAPITAL FORMATION"

TUESDAY, MAY 10, 2011

Good afternoon. I wish to thank Chairman Issa, Ranking Minority Member Cummings, and the other distinguished Committee Members for the invitation to testify today. My name is Roel Campos. I am currently a partner with the national law firm of Locke Lord Bissell & Liddell LLP where I practice securities law, representing businesses and individuals. I come before you not as an advocate or expert on the particular regulatory changes that the Committee has posed to the Securities and Exchange Commission ("SEC"). Instead, I testify today from the perspective of a former SEC Commissioner. Like you and the SEC currently, during my tenure as SEC Commissioner, I often faced the difficult challenge of how best to reform and improve securities laws and regulations. I learned first-hand how difficult it can be to balance the goals mandated by Congress: protecting investors, but also facilitating capital formation, and preserving the integrity of the markets.

With your permission, my testimony today has two modest goals:

(1) Presenting a short discussion of the factors and considerations that must be balanced to produce sound regulations; and
(2) Offering observations and suggestions to assist the SEC to achieve appropriate reform of current securities regulation.

As you know, I had the privilege and great honor of serving as a Commissioner of the SEC. Confirmed twice by the Senate, I was in office from 2002 to 2007. During my tenure, like today, the SEC faced the aftermath of a serious financial crisis from the scandals presented by the cases of ENRON, WorldCom, and others. Then, like today, Congress passed major legislation to deal with the abuses that occurred—the Sarbanes-Oxley Act of 2002. Today, like then, the SEC faces the aftermath of the severe financial crisis in 2008, and Congress has passed another major piece of legislation—the Dodd-Frank Act Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), directing the SEC to implement Dodd-Frank.

First, let me begin by briefly discussing "investor protection." In my experience, this concept, when raised, regularly produces cynicism and the disbelief that this is a serious goal in today's complex environment. Many seem to believe that the concept of investor protection is archaic and long ago ceased being useful—that it is a musty relic of a bygone era, the market crash of 1929. I respectfully disagree. I submit that investor protection remains today as important as it was 80 years ago, when Congress made it the fundamental underpinning of the securities laws. As a Commissioner, I was often asked with respect to investor protection, "What investors exactly? And, do investors really need that much protection?"

Certainly, the term "investor" is very broad. Congress and the SEC have never made a distinction among the different categories of investors, which include: institutional investors (*e.g.*, pension plans, which represent public and private employees), professional investors (*e.g.*, private asset managers and hedge funds), and finally retail investors—the everyday person who holds a brokerage account or tries to manage his/her retirement plan.

During my tenure at the SEC, I was privileged to represent the agency in the international arena, where I learned first hand that our markets are unique. Securities markets in Europe and Asia are comprised almost exclusively of institutional and professional investors. In the U.S., however, retail investors provide a significant portion of the capital that is invested. Retail investors thereby add a depth of liquidity and offer a diversification of investor base to U.S. markets that cannot be found elsewhere in the world. Indeed, the liquidity and diversity of the U.S. markets help convince many foreign investors to invest in the U.S.

When I was a Commissioner, I worried most about retail investors, as institutional and professional investors have strong associations and lobbyists to present their views and needs to Commissioners and SEC staff. As for the vast majority of the American public, few speak on behalf of the "retail investor" to Congress or the SEC. Protecting investors is certainly rooted in equity and justice. However, there are other fundamental reasons for protecting investors. America needs investors to participate in our markets without fear of being defrauded or being victim to tricks and stratagems. If U.S. markets are viewed as "unsafe," all categories of investors will abandon our markets.

This is not idle worry. After every scandal or malfunction of the capital markets, investor confidence is damaged and retail investors in particular leave the market and stop buying equities and other securities. The recent financial crisis in 2008 demonstrated this, and studies show that retail participation has not yet returned to pre-2008 levels. Consequently, if our markets experience a sustained loss of investor confidence, they will permanently lose liquidity and cease to be the source of capital to drive growth and jobs for our economy. Without deep and vibrant markets, America's economy will most likely stagnate and produce a lower standard of living for its people.

But there is yet another consideration: Americans today must mostly fend for themselves and self-manage their retirement savings. Most of us do so through 401(k) plans that require us to make investment decisions. Gone for most Americans are the days when their employer maintained an employee pension and guaranteed a particular defined benefit after they retired. Surely, Congress and the SEC owe the vast portion of our population safe and stable markets that are free of fraud or mischief and in which they may choose stocks and debt instruments to maintain themselves in their elder years. For all these reasons, investor protection should not be taken lightly, and its consideration is vital in any reform of securities regulation.

A second principle is that regulation that protects investors does not impede capital formation but instead attracts capital. I remember vividly, as a Commissioner, when one European institutional investor told me: "I invest hundreds of millions of dollars in equities in America because I consider American markets to be the safest in the world." During my tenure, I debated and contrasted U.S. markets to other jurisdictions, such as the U.K. and others, that maintained what was regarded as a "light touch regulatory regime." I defended U.S. markets and argued that America placed, as its first priority, the protection of capital and that this principle would continue to be a magnet for capital from around the world. I argued that the primary concern of any regulator had to be the safety of capital and that the financial services professionals would follow the capital. It is clear today that the U.K. and other jurisdictions have revised their views and imposed on their markets a system of regulation that also places investor protection at the top of their priorities. Again, capital finds the markets where it is best protected.

There is a danger in accepting, without careful analysis, the view that U.S. markets are in some type of major decline. I agree that there are currently significant challenges to our markets. However, statistics showing that foreign IPOs in the U.S. have declined must be interpreted in the context of the global economy and on a longer timeline. There was a time when the U.S. markets were the only source of capital for large offerings. During the recent past, the number of large pools of capital, including sovereign wealth funds, in Europe, the Arab world, and Asia grew tremendously. Companies do not have to come to the U.S. to raise capital. Moreover, studies show that the natural shareholder base and constituency for any public company will be those living within the geographical region in which the company has its principal places of business.

I therefore believe that some comfort can be drawn from those statistics, which show that foreign companies continue to view U.S. markets as an attractive source of capital, and many issuers still choose to list on U.S. exchanges even though they do not need to raise capital. In fact, registering in the U.S. provides foreign companies the opportunity to use their shares as currency to acquire American companies for strategic growth. More acquisition opportunities exist in U.S. markets than in most foreign markets. In addition, one cannot ignore the large amount of capital that is raised in the U.S. through private placements in which many foreign companies participate. And, finally, U.S. exchanges have become international in their operation or have foreign exchanges as partners, and U.S. investment banks participate vigorously in Europe, the Arab world, and Asia and benefit from the capital raising activity in those regions. All of this, however, lessened the need for foreign issuers to pursue IPOs in our country.

A third principle to keep in mind is that the SEC has always been open to improving its rules and regulations. The business on Main Street, the capital markets, and technology constantly change; oversight continues to adapt to such changes. During my tenure as a Commissioner, I wrote an article supporting Securities Act reform to enable more efficient offerings and improve the ease of raising capital. I was elated when the SEC's Corporate Finance Division formally recommended Securities Act reform, and many of the ideas that I had supported were ultimately adopted. Also note that there are many other examples of the SEC taking initiative and tackling areas of regulation that needed reform. One of them was the SEC's efforts to modernize the markets through the adoption of the National Market System, which offered new transparency and efficient access to the best price, regardless of the market. As testified by Chairman Schapiro, the SEC is ready and has a history of being open to ways of improving rules and regulations.

Obviously, there has always existed, and continues today, deep annoyance that the SEC takes too long to consider new ideas and recommendations for improvement. Frankly, the reason it takes so long is that there is almost never widespread agreement on any proposal. Business interests often have competing stakes in the respective business models and disagree among themselves. Add to the mix that investor groups do not easily abandon rules that have offered transparency and protection, and consequently, they therefore often pose substantial objections to changes. Finally, the decisions that must be made are truly complex and any solution will of necessity be viewed as negative by some participants.

Moreover, consider that the SEC is an agency consisting principally of lawyers. However, the skills and training that are needed to evaluate capital formation or the efficiencies and working of the markets are often not those of lawyers. Clearly, the SEC needs more economists, statisticians, financial researchers, and those with experience in the day-to-day workings of the markets and computer systems that are currently used in the markets. In my role as international Commissioner, I was struck at how other countries viewed the regulation of their securities markets as a top priority. To that end, governments regulating financial centers such as London or Hong Kong offer their senior staff compensation that is comparable to the levels of the private sector. That is in stark contrast to the approach in our country, where there is little consideration for the need to attract the regulatory and financial talent necessary to respond appropriately and confidently to the complex demands from many constituents. It seems to me that investment in resources at the SEC could allow the agency to respond more efficiently and confidently to the demand for approval of new financial products as well as to study and recommend regulatory improvements.

I realize that Congress is in no mood to increase funding for any part of government, much less for the SEC. However, the irony is that the improvements and efficiencies of the type that this Committee demands can only occur on an expedited basis if additional resources are brought to bear. Appropriately skilled staff could perform more rapidly the necessary studies with correct statistical significance, evaluate the costs and benefits imposed by its regulations, study commentary by the market participants, conduct follow-up surveys, and properly weigh investor protection with the resulting efficiencies in capital formation.

A concept that I have viewed favorably is the establishment of a permanent citizens' advisory board for the SEC that would include members of the regulated industry, public companies, and investor representatives. The Fed has such a board. This advisory group should have resources and be supported by SEC staff. One could jump-start and incorporate into this board the SEC's long-standing use of outside groups of distinguished individuals who present well studied suggestions for improvement of regulation. Relying on an advisory board, however, will not speed up consideration of new ideas for reform. Its limited resources and its members' limited and voluntary time will by necessity not suffice to efficiently and promptly draft sound regulations.

Another approach that may seem heretical, but that deserves consideration, is permitting the SEC to raise the fees it charges registrants and other users of its services. Such additional revenue, subject to scrutiny and budget requirements, could be used to expand the SEC's capacity to efficiently consider new reforms. Congress could certainly specify the particular subject areas and studies that could be funded from such additional revenues to assure the focus it desires.

Ultimately, I agree that there are many areas of securities regulation that demand substantive attention for improvement and reform. In addition to the areas raised by this Committee, many have pointed out that the workings of the markets need new study. To many, the recent flash crash has not been satisfactorily explained. The full impact of the use of computerized trading has not been fully studied. Further, many worry that despite improvements in regulations, such as Reg SHO and 204T, the markets still seem vulnerable to manipulation from failure to deliver shares after short sale orders of exchange trade funds (ETFs). Others worry about the serious fragmentation of the markets and the existence of untransparent dark pools. There are certainly many other areas of concern.

Again, without additional resources, it is difficult to see how the SEC can accomplish all of the mandates of Dodd-Frank and study new ways of facilitating capital formation, as well as oversee markets that are dominated by giant computers doing analysis and trading in nano-seconds.

Business and the financial services community need a smart twenty-first century regulator. Other jurisdictions view investment and market-competitive compensation for their regulators as an important contribution to help their markets attract capital. In the United States, we should have the same view.

Thank you very much for your kind attention. I am happy to answer any questions you might have.