

The Economic Club of New York

289th Meeting
73rd Year

The Honorable Benjamin R. Civiletti
United States Attorney General

Arthur Levitt, Jr.
Chairman of the Board of Governors
Chief Executive Officer of the
American Stock Exchange

June 26, 1980

New York Hilton
New York City

Questioners: Mark Kaplan, Partner
Skadden, Arps, Slate, Meagher, Mohr, and Flom.

Thomas Macioce, President
Allied Stores Corporation

Introduction

Chairman Edmund T. Pratt, Jr.

Welcome to this, the 289th dinner of the Economic Club of New York. I am Ed Pratt, your chairman for this season. This is our third dinner meeting in the Economic Club's 73rd season and I certainly hope you've been enjoying our programs this year. It's all covered in the program, but I'd like to mention again that we do indeed have a unique club here which has grown over the last 73 years by doing just one thing – by presenting to the New York business community the views of American and world leaders from many fields. We can all be proud of the Club's reputation as one of the world's major speaking platforms.

You will be happy to know as members, many of you, that the Club's membership continues to grow and that the Club's financial position has been greatly strengthened – I think a very appropriate thing for an economic club. I hope that you members will continue to encourage other executives in your companies to become members. As you know, membership is by individual and not by company. May I suggest that you chief executives and other senior executives propose or second for membership others in your organization so that they may enjoy the opportunity of hearing national and world leaders discuss the key issues of our time.

We are especially pleased to have as speakers tonight two distinguished leaders – each obviously brings expertise from a different field. It is traditional for two distinguished representatives of the

business community to represent the audience by posing questions to our speakers. As questioners for our speakers this evening, we are fortunate to have two outstanding New Yorkers who are also members of the Economic Club. Our first questioner is Mark Kaplan, partner of Skadden, Arps, Slate, Meagher, Mohr, and Flom. And our second questioner is Thomas Macioce, President of Allied Stores Corporation.

Let me now introduce our first speaker, Attorney General Benjamin R. Civiletti. He was born and raised just north of the city, in Peekskill, so we're glad to welcome him home. Graduating from the University of Maryland Law School in 1961, he served as a law clerk for the Honorable Calvin Chesnut of the US District Court of Maryland. From there he became Assistant US Attorney for the District of Maryland. Soon thereafter, he joined the law firm of Venable, Baetjer & Howard in Baltimore. He shortly became a partner and then was made head of their Litigation Department. It was logical then that Benjamin Civiletti's first Justice Department position was head of the Criminal Division. Within a year he was chosen by President Carter to the post of Deputy Attorney General. And on August, the 16th of 1979, he became the 73rd Attorney General of the United States.

The Attorney General has not only had a distinguished legal career but a career marked by service to his profession as has been recognized by the awards made to him. Among the honorary awards and decrees are the Herbert H. Lehman Ethics Award, an election to the status of Fellow in the American College of Trial Lawyers. He has received Honorary Doctors of Law

degrees from the University of Baltimore, New York Law School, St. John's University, Tulane University, Notre Dame University, and his alma mater, the University of Maryland. It's no wonder that Benjamin Civiletti's predecessor, Griffin Bell, has called him the lawyer's lawyer. We are honored to have him here tonight and I present to the Economic Club of New York, the Attorney General of the United States, the Honorable Benjamin R. Civiletti. (Applause)

The Honorable Benjamin R. Civiletti

Attorney General of the United States

Thank you very much Mr. Pratt, members of the dais, and members of the Economic Club of New York. It may be typical of the Justice Department that I come to the Economic Club of New York, the most prestigious club with the most outstanding members in business, finance, and industry prepared to speak about small business. That sounds a little bit like the Department of Justice and the manner in which they achieve the appropriate action for the appropriate occasion.

But Arthur and I discussed it more than two or three months ago, and since he had recently served on, and served well, on the commission with regard to small business, I was under the impression, and perhaps foolishly, that occasionally big business likes to hear about small business. I have tailored my remarks to some extent and abbreviated them, thank goodness, so that they will serve merely as an appetizer to the main meal, which I enjoy much more and I trust that you will, which is the question and answer period.

There are certain subjects, of course, which I deal with which are routine, of little interest, and of course to which I cannot respond. Abscam is one, Ramsey Clark is a second, (Laughter) Iranian assets, which are frozen or almost frozen or subject to suit on frozen assets is a third, Haitians is a fourth, Cubans are fifth, whether or not there are going to be any revisions in the tax laws is the sixth – and that's one I really know nothing about – and on and on. But I trust that the interrogators will not be intimidated by my setting up those straw men in attempting to knock them down.

I will chat with you for a few minutes about two aspects of business prospects, and particularly since we prepared it, and it took a lot of effort, forgive me for the extent to which it falls over into and relates to small business, prospects for the next several years and to some extent perhaps for the 80s. With regard to small business, despite gloom and doom predictors, it seems to me that small business is healthier today than it has been in the past. Small businesses, and I won't bother you with various definitions, have grown in size, increased in number, have become profitable, and continue to provide an enormous number of jobs. And after all, it is small business that grow, develop, and become medium and big business.

I won't numb you with statistics, but I'll cite just two. A survey and study of 45 of the nation's 440 manufacturing industries shows that in terms of a high percentage of these manufacturing industries, the small firms are operating at levels of profit more than comparable with large firms. The Federal Trade Commission figures reveal that after-tax returns on equity were higher

than the national average in all but one of the quarters of 1978 and 1979 for manufacturing corporations with assets of under \$5 million, and all but two of those quarters for manufacturing firms with assets of between \$5 million and \$10 million – certainly under anybody’s definition, small, small businesses.

It can’t be denied that big businesses usually dominate those markets where large scale is essential for production, where substantial funds are needed for continued applied research, or where capital investment on a substantial scale is required for entry. But if we put to one side those kinds of markets or industries, we find that small businesses and medium businesses play a very important role in manufacturing. Thus, there are many markets where the economies of small scale production and the flexibility within it can be efficient, can be productive, can grow and prosper despite the limitations of size. For that reason, small businesses are prominent, as you know far better than I do, in the fabrication and manufacture of highly specialized projects and are able to more than match big business.

But let me turn, after that brief reference, to two aspects of business and the federal government which cause continuing concern, believe it or not, both within the government and certainly within the business community. Two of those most important aspects are taxes and regulations. I believe and trust that we will see increasing recognition by both the Congress and the Executive Branch of the importance of tailoring our federal tax laws so as to avoid unfairly penalizing or shortchanging or encumbering business. I will have more to say about regulation which is dear to

my heart in a moment, or perhaps deregulation.

But with regard to taxes, for example, the administration has supported and obtained enactment, as you well know, of a permanent increase in the investment credit from 7% to 10%. It was due to a decline to 7% this year. In response to an administration proposal in another area, the Congress expanded certain provisions which encourage investments in small corporations by allowing ordinary deductions rather than the less favorable capital loss treatment for losses sustained by an original purchaser of corporate stock. For example, each small business is now allowed to issue a million dollars of such stock as opposed to half that amount under the prior law and thus investors of all kinds are encouraged to invest up to million dollars in a business knowing that if the investment fails, the total loss may be taken as an ordinary deduction.

Concern over estate taxes has contributed importantly to the demise of many small businesses and as importantly, if not more importantly, to hardships on major stockholders who have desired to have their estates in some substantial form of liquidity. Recent changes in the estate tax law have helped lessen and remove some of the inequity with regard to the estate tax burden. Most estate taxpayers now pay no estate tax on estates valued at less than a quarter of a million dollars. But more importantly again, Congress recently reinstated the old rule under which for capital gains tax purposes, the cost basis for inherited property is the value at the time of death rather than the old rule of, or the current prior to the amendment rule, of cost.

Lastly, with regard to taxes, the administration is working today with the American Bar Association, your state bar association, the New York State Bar Association, and the City Bar Association of New York to structure a reform bill to simplify the taxation of deferred or installment sales of property. In particular, the bill would eliminate the often troublesome requirement that prevents this favorable tax treatment of payments in the year of sale where it exceeds 30% of the selling prices.

Let me move now from that brief glimmer with regard to taxes, to government regulation which is, I think, a primary concern of all businesses. Here again I think there is some reason for optimism. The administration and the Congress are working together to eliminate, or to try to, and to reduce regulation in a number of the most heavily regulated industries in our economy. These efforts have already resulted in significant deregulation of the airline industry, both passenger and cargo, and should soon lead to regulatory reform in important areas of the motor carrier and rail transportation industries. While it is commonly perceived that the primary beneficiaries of deregulation are big companies, I would suggest that small businesses and medium businesses have at least as much to gain. Indeed, they often find themselves disproportionately burdened by industry-wide regulations.

Last November, President Carter directed the heads of executive departments and agencies to use flexible approaches to regulate small businesses and medium businesses. He directed us to tailor regulatory and reporting requirements to fit not only the size but the nature of the businesses

subject to them. For the most part, health and safety regulations are intended to promote goals on which there's an overwhelming consensus in our society regardless of whether you're in business or in professions or in service organizations, in government or institutional endeavor.

Yet, even regulations designed for uncontroversial purposes of public betterment can often have very controversial and unintended results. Because our society believes so firmly in equal treatment under the law for both the great and the small, there is a natural and perfectly understandable inclination to achieve uniformity in the regulatory process. But that instinct overlooks other factors. Suppose, for example, we're talking about air pollution. It may well be that in any given industry or line of commerce 80% or more, 90% of the pollutants are discharged by only 10% or 5% of the organizations engaged in that industry or line of commerce. Subjecting all companies in the industry to the same regulatory requirements means that obligations for very costly capital investment in new equipment and for high maintenance cost will devolve upon businesses of all variety and sizes, depending on their share of the market, which can ill-afford those outlays at a time when they are struggling in one way or another to become competitive. Thus, perfectly sound regulations applied indiscriminately would result in economic effects which are not only unjust but are also in-amicable to the value which we all place on free and broadly-based competition.

We ought to aim at a just outcome for society and all members of it at large rather than at a deceptive, formal justice in the application of seeming uniformity. The administration is now

moving in that direction by a process which has been labeled or known as tiering which fits regulations to, and hopefully with some sense and reason and less arbitrariness, the size and nature both, of regulated businesses. For example, the Environmental Protection Agency has used tiering to require less stringent pollution control levels. In addition, it has granted outright exemptions to sectors of industries whose economic position, or the nature of whose business is such as to be precarious, but which contribute little in the overall perspective to the pollution problem which is attempted to be addressed. It is my firm belief that the balancing of society's regulatory goals in this way is a healthy and more just way of proceeding than the apparent justice of perfect uniformity and equal arbitrary application.

Thus far I've been speaking of health and safety regulations as distinguished from economic regulation. By economic regulations, I refer to statutes and regulations adopted thereunder which both limit entry and regulate competition among those businesses licensed to compete in a given market or industry. The de-regulatory mood of the Congress and the administration aims at substituting competition for government regulation as the market determinant. Increased reliance on competition and the free market choices on industry and initiative will enhance prospects for business in almost every way.

First, it provides new opportunities. There's a tendency in certain regulatory schemes to favor companies already there, to maintain the status quo, to be regulated at the expense of new entrants whether they are new companies or whether they are new enterprises of old companies.

This almost always works to the disadvantage of the entrants, and particularly small businesses that are potential entrants into these industries.

A prime example of regulatory form which we have all studied and become familiar and which will be the source of studies for years to come that ease the burden of small businesses seeking entry into a regulated industry is the '77 legislation that substantially deregulated the air cargo field. On the passenger side, in the Air Deregulation Act of '78, Congress directed the Civil Aeronautics Board to consider specifically “strengthening small air carriers so as to assure a more effective, competitive airline industry. The Motor Carrier Reform Act of 1980 which recently passed the Senate would reverse the burden of proof in motor carrier entry application so that opponents of new entry would have to demonstrate that the proposed services were inconsistent with the public convenience and necessity. These and similar reforms will give many more businesses a fairer chance to gain entry into regulated industries and will provide for the survival of the strongest according to market demands, according to service, according to efficiency, according to price, and according to customer preference.

Second, deregulation promotes flexibility and efficiency. In the trucking industry, for example, a combination of regulations prevents truckers from back-hauling in certain circumstances, forcing trucks to return empty after making deliveries although cargo was available and the truckers are willing to haul it. That makes no sense, practical or economic or in any other way. And this type of restriction is particularly burdensome to small businesses that must perform at maximum

efficiency to prosper.

The pending Motor Carrier Reform Act of 1980 would eliminate or change a number of current regulations to make it easier for truckers to back-haul cargo. Moreover, small businesses that depend on motor carriers to ship and to deliver supplies or products to market will benefit directly from the flexibility being afforded truckers to serve new routes. If the shipments are there, trucks will be ready and willing to carry them. Shippers also will not have to worry about rates being inflated by anti-competitive agreements.

Let me turn now to the necessary concomitant of deregulation – reliance on competition and solid, evenhanded antitrust enforcement. A necessary result of an enhanced competitive environment is increased pressure on inefficient businesses and a certain amount of disturbance of the status quo. While most businesses truly favor deregulation to the greatest extent possible and are willing to accept the increased uncertainty in exchange for the greater opportunities for success available in a competitive economy, free of bureaucratic regulation, some may prefer the easy life and protection against competitive inroads.

However, those who want to take full advantage of the competitive freedom that deregulation provides – for example, by lowering prices to attract customers that we are seeing in passenger airlines or by marketing new products and services – are fully protected instead of victims or subjects to, are fully protected by the antitrust laws. Attempts by others to squelch innovative

business behavior through, say boycotts, of the offending company or its customers, would be and is illegal per se. I am firmly convinced that a competitive economy favors the growth and prosperity of all business and that the antitrust laws are a key factor in the prospects for business success in a deregulated arena.

That the antitrust laws are in many ways the antithesis of regulation is a point often missed by people unfamiliar with them or who have suffered a poor experience perhaps under them. The resourcefulness, the innovation, the efficient businesses – large and small – are free to do as they will so long as they stay within rather broad boundaries established by the antitrust laws. Within these boundaries, their judgment and the judgment of the marketplace are not reviewed by any regulatory or bureaucratic agency or department.

In my opinion, a competitive system protected by antitrust enforcement is particularly vital to small businesses or new areas of development. Because of their lower overhead and smaller staffs, because of smaller investment, smaller firms or enterprises are often better able to adjust to new concepts and to introduce new products and operational practices. They need room to innovate and expand, whether they're small businesses or they are new subsidiaries or new ventures from a large business. They need to be able to enter markets easily and to be free to shift resources into new areas in response to changing market conditions.

Vigorous antitrust enforcement creates this type of environment. Take for example the recent

litigation against manufacturers of folding cartons, corrugated containers, and consumer bags, these are purchased by businesses of all sizes, of all varieties, and of all products to package their merchandise and their products. The Department of Justice's efforts have resulted in criminal convictions as well as injunctive relief. Victims, and there are many of these conspiracies including numerous large and small businesses, who were in effect cheated by these price-fixing schemes, have recovered hundreds of millions of dollars in damages in private cases ancillary to and following the Department's prosecutions.

I conclude with this observation. As the Chief Law Enforcement Officer of the United States, I am dedicated to the rule of law. There is a dangerous tendency, I think, abroad in the land to try to solve our problems with mindless, quick fixes that weaken the rule of law and our basic economy. Moreover, we have a tendency as a people to dump too many of our problems into the courts. Thus, creating an unmanageable maelstrom of federal court litigation. And no one, I suggest, knows better than those of us who have devoted our lives, professional lives, to litigating and who give as the soundest advice to clients and generally, with some of the very best litigators to corporate clients who are subject to such suits, the difficulty and unpredictability and the expense and sometimes senselessness of such litigation.

Some people believe that the devils in this picture are the regulators at the Washington agencies. Congress appears to believe that the devils can be exorcized by so-called legislative vetoes of agency regulations. With all due respect to the Congress, I believe that this so-called solution

won't work, that it is unconstitutional, and I have so advised the president.

We are, of course, bound to continue to rely to some degree on government regulation of business, including large and small business. But wherever possible, wherever possible, I believe we should place our chief reliance on market forces to regulate competition and not government agencies. I am convinced that business has the most to gain from free competition because of its, not only great flexibility and adjustability, but from the energy and imagination and incentive of businessmen and not government bureaucrats. Thank you very much. (Applause)

Chairman Edmund T. Pratt, Jr.: Thank you Mr. Attorney General. And as a matter of fact, we appreciated those helpful comments to small business because most of us up here in little old New York are just little old companies struggling to stay ahead, and we appreciate all the help we can have from you. We're anxious to get to some of those straw men.

But before we do, I'd like to introduce our second speaker, Mr. Arthur Levitt, Jr. Arthur is Chairman of the Board of Governors and Chief Executive Officer of the American Stock Exchange. Prior to his election as AMEX Chairman on December, the 30th of 1977, he was President and a Director of Shearson, Hayden, Stone, Inc., a New York-based securities and investment banking concern.

In addition to his business achievements, Arthur has devoted considerable effort and time to

public service. He admirably follows in his father's footsteps, who as Comptroller of the State of New York for so many years was known as the People's Auditor. In 1978, President Carter named Arthur the Chairman of the White House Small Business Conference Commission. He has served the business community and our city in other capacities, including membership on the American Council for Capital Formation, the Advisory Board of the Securities Regulation Institute, the Downtown Lower Manhattan Association, and the Advisory Council of the New York University Finance Club. He's also a Director of the East New York Savings Bank.

Arthur has also made a significant contribution to the community outside of business. As a delegate to the New York State Constitutional Convention in 1967, he served as Chairman for the Conservation Committee and in that capacity wrote and sponsored what has since been referred to as a Conservation Bill of Rights. A large part of the body of New York State conservation laws we have today are a result of his efforts at the convention and since then. His varied interests have also extended to the arts as well. Arthur has served on the New York State Council on the Arts in 1970, 1973, and 1978.

This combination of interests has made Arthur Levitt, Jr. a recognized leader in our city and the country. We are pleased to welcome him to our dais, Mr. Arthur Levitt.

Arthur Levitt, Jr.

Chief Executive Officer, American Stock Exchange

Looking forward to sharing the platform with the attorney general, and speaking before the prestigious representatives of big business, I asked my associates to help me work up a draft. It came back loaded with economics and complicated theories about what the Fed should be doing, what the president should say, what the Congress should enact. It sounded important and I suppose it was. But it was dull, very, very, very dull. There wasn't even a joke in it. There was nothing, absolutely nothing about my feelings in it. But, Arthur, my associates pleaded, Arthur, this is what they want to hear. This will be a sophisticated, educated, erudite, tuned-in, with it audience. This is what they expect. Besides, they're busy people and maybe they could use a little sleep. Go on, give the speech. (Laughter)

No, I said, this is an opportunity to tell this sophisticated, intelligent, erudite, tuned-in, with it audience something they may not know, but should know about how I believe the economy of this country really works, a thing or two about what's going to make it better, a more effective way for us business people to take advantage of the growing common interest between labor and management to raise productivity, to create jobs and whip inflation. That, I figured, would get your attention. Besides, I like to think of myself as something of a risk taker. How can I possibly say I'm a risk taker if I won't so much as take this opportunity of telling you what I want to tell you rather than what others tell me you want to hear.

Running risks really is what business is all about. But it seems to me that in recent years the risks have grown much greater and the rewards much harder to find, if in fact we can find them at all. The result, I think, is a tendency to avoid risk, to find ways of operating without risk, almost but not quite a fear of it. In politics, play it safe politicians cater to the thousands of single issue constituencies instead of addressing the nation's needs as a whole.

In money management we have the deadening influence of ERISA, the institutionalization of the prudent man, and the herd instinct of doing no better than average. Especially in economic policymaking we see the desire to avoid risk. For months the Washington money men and women have been acting politically in response to campaign requirements just as they did in '64, '68, '72, and '76. Go on, they say, it's okay to use your credit cards again, only three months after they said to put them away in a drawer.

Unemployment is going up faster than we had expected, they're saying. So let's spend some more money, some more federal dollars to create jobs – again just a short time after cutting spending seemed to be the cause of the day. And yes, maybe we do need a tax cut after all. In March, the president said the administration couldn't afford policies to stimulate entrepreneurship until the budget was balanced. That kind of confused me. It seemed to me that perhaps it might have worked the other way around. First, the stimulus for entrepreneurs, the risk takers, then the balanced budget. Now, of course, it looks like we may get neither.

We're not really sure where the administration is getting its economic advice these days. Perhaps a story I heard recently may be true after all. I was told that last May Day as Mr. Brezhnev was reviewing Russia's military might, he kept nodding with approval as the infantry divisions marched by and the thousands of missiles rolled on and the hundreds of tanks rumbled through Red Square. But after the tanks, then came a thin line of 12 gray-haired men dressed in blue suits with attache cases. Brezhnev's face clouded over, his brows knit with doubt. What are these, he asked his military commanders. Are they spies, asked Brezhnev. No, said the head of the Russian armies. They're economists. You have no idea, Comrade Brezhnev, how much damage they can do. (Laughter and Applause)

But the problems of our economy, whether they're introduced by stop-go-ism of our economic policymakers or by some endemic weaknesses that have grown malignant over time, make it appear that there really is no place for individual risk takers. Is that in fact really true? No, I think not. Certainly not in my world of small business and mid-range companies. Why is this my world? Why is the chairman of the nation's second largest exchange speaking for smaller companies and on behalf of individual investors? Basically because I believe that securities exchanges that speak and act only in the interest of a tightly-knit, narrowly controlled, self-perpetuating membership have no relevance either to the needs of the nation or the mandates of the Congress. Those institutions that remain merely the passive domiciles of companies whose shares are traded on their floors will soon go the way of the buggy whip and the 5-cent cigar.

I passionately believe that the liquidity resulting from a national re-commitment to equities will develop only after the return of the millions of retail customers who since 1973 abandoned common stock for such non-productive investments as precious metals, index funds, and exotic collectibles. According to Dun & Bradstreet, more than 477,000 new businesses were incorporated in 1978. And late in 1979, the annual rate was running at more than 520,000, 63% greater than the number of new incorporations only five years before. Business is one of the last, if not the last, staging areas for risk taking in American life – the last frontier if you will – of a nation that at one time was nothing but frontiers.

Let me tell you just a little bit about the risk taker – the individual American entrepreneur. There are 12 million of them in the country today. And these millions of small businesses account for just about 40% of the gross national product. And if you think that nearly all the inventions come out of big industrial laboratories, think again, for half of all inventions from 1929 to 1969 came from firms with fewer than 1,000 employees. It's often very easy to overlook this side of our economy, and I guess this city is a good example. New York City certainly doesn't look like it's a small business town. But no matter how you approach it, by air, sailing into the harbor, arriving by highway or rail, you're enveloped by topless skyscrapers bearing the names of some of the world's most famous multinational corporations. But let's take a closer look.

Pan-American occupies only 11 floors of the Pan-Am building, 250 small companies occupy the

other 45 stories. Only a fifth of the Seagram building is, appropriately enough, occupied by Seagram's, (Laughter) 120 companies do business on the other 30 floors. And Chrysler doesn't live in the Chrysler building anymore but hundreds of other smaller firms do. Last year, MIT did a study on just how jobs were created. It's the individual firms, they found, that generate jobs, export products, and utilize natural resources. And what kind of individual firms did they discover were doing all this? Small ones, flexible, energetic, and creative. Small ones accounted for nearly 86% of the new jobs created in this nation every year.

My point is simply that small business is really the leading edge of growth in our society. By increasing the nation's productivity, it can put pressure on prices, lower inflation, and help restore America to competitiveness in world markets. But let me say also at the same time that small and large businesses are not fundamentally antagonistic. They are, in fact, mutually dependent. For instance, General Motors has 40,000 suppliers, most of them small businesses. General Electric's major appliance division buys 30% of its products from small business, its airplane division, nearly 40%. And much of the same can be said of almost every major company throughout the land.

Big and small business have more in common today than ever before. I speak particularly in terms of public and legislative credibility. Today big business speaks for all business in America. But small business can become an important partner in achieving business objectives. Rightly or wrongly, to be big in America is also bad in the public's view. Small business doesn't have that

problem and can more easily and persuasively argue for reforms that will eventually help all members of the business community. Small business is so varied, so peppered throughout the American economy that it's been difficult to recognize its contribution, harness it, and provide it with the necessary encouragement. But provide it we must. If these small business people are among America's last risk takers and last technological adventurers, then we will indeed be in trouble as a nation if they are not permitted to prosper. From my perspective, there are no quick and easy solutions to our problems. Having said that, I would go on to offer some suggestions that could do much to nurture not just young and growing companies but the entire business community, and indeed the nation's economy.

One, discipline government spending. Business should no longer have to compete with government for the limited money resources of the nation. To do so is exhausting and wasteful and sometimes ruinous to small enterprises.

Two, limit the tax burdens. These have an inhibiting effect on all business activity. They corrode investment, production, and employment, and they hurt the formation of all new businesses. We must put first things first. First, limit spending and taxes, then draw up a federal budget that we can live with, not the other way around. And once that's accomplished, we've got to renew the trend of reducing taxes, and a good place to start would be a further reduction in the capital gains tax. This will benefit everyone, especially small and medium-sized, growth-oriented companies.

And next, let's give serious thought to reducing the tax on unearned income as a way of further stimulating incentives to save and invest. In this connection, our tax code has an anti-savings, pro-consumption bias that permits an individual to deduct from taxable income every penny of interest paid but forces him to pay taxes on every penny of interest earned. This bias is so deeply ingrained that few people seem to notice it anymore. Tax considerations then make it more attractive to buy a house than to put money into common stock. This creates a huge capital bias towards housing rather than for instance plant and equipment. What was once a sacred cow is now milking the free enterprise system. Might it not be time to think about allowing home mortgage interest deductions only below a certain level, let's say \$100,000?

Third, limit the money supply. The philosophy in Washington should not be how much you let up on the accelerator, but really how much you depress the brake. The money supply should not be allowed to exceed growth and productivity and real output.

And fourth, limit the scope and growth of the federal regulatory establishment. Of course, retain those regulations that protect the public in terms of health and safety, but curb the agencies whose growth has obviously exceeded their original mandate and purpose. During the 70s, all too often it seemed that the truly successful entrepreneurs in our society, the real empire builders, could be more easily found in the burgeoning public sector than in the private sector. I strongly believe that in the 80s we must seek to replace bureaucratic entrepreneurship with business entrepreneurship. That was the real message of the recently completed White House Conference

on Small Business.

And lastly, I think that we should recognize the essential interdependence of groups that have very often been thought of as having adversarial interests. For instance, if there are any in this nation that should naturally be together on an issue such as incentives for economic growth, it should be labor and management. But that's just not happening. We need to be able to jointly carry our message to the Congress and to the public that an automobile plant that shuts down hurts all of us, and that incentives for entrepreneurs and for capital investment can help all of us.

If the politicians haven't been as responsive as we may have liked, the fault may well be our own. For far too long the business community has advocated its own interests to the apparent exclusion of other constituencies. In our system, if one appears to be advocating one's own interest as opposed to, say labor, or the interests of minorities, you're just not going to get enough political support to accomplish what you have to accomplish. In fact, this inability to resolve problems is the subject matter of a provocative new book called *The Zero-Sum Society* by Professor Lester Thurow of MIT. He focuses upon the veto powers held by key economic groups in our society and the stalemates that so often occur in the shaping of national policy. His recommendations for reform are controversial and in many instances shortsighted. But he does put his finger on the fact that for progress to occur, conflict must give way to consensus.

I agree that it's absolutely necessary that whatever we have to do, we must indicate that we, as

Americans, are in this together. And if our economy grows, all of us are going to benefit. And if our economy shrinks, all of us will suffer. We must have a common message and a common objective. All too often when we in business talk about productivity and capital formation, labor automatically grows apprehensive and may even oppose them. But politically that really puts us in a very difficult spot. I think that we in this nation have to make a basic decision as to whether we're going to continue to fritter away our resources and dissipate our strength. If we're going to grow, that's a decision that all of us are going to have to make.

We're going to have to talk about it. We're going to have to debate it. And we're going to have to start meeting together, labor, management, business, and yes even the so-called special interest groups, to try to map a common strategy. Because unless we do, we're just going to continue down the same slippery slope that we're on right now. That we are not antagonists is beginning to be recognized by any number of disparate groups. Capital formation has become a matter of compelling concern to some of those who in the past have viewed this as a privilege for the poor but the privilege for the rich paid for by the taxes of the poor. The head of a giant municipal employees union has said that private sector jobs are a key to soaring urban troubles. The Black mayor of Los Angeles testified on behalf of the AMEX bill that gives a tax credit for investing in smaller companies. Prominent members of minority groups are calling for a re-emphasis on capital formation.

So in spite of all our problems, entrepreneurship is still alive although not so well as it might be.

It is, when you come right down to it, remarkably resilient. We've got to keep it healthy. There are still an awful lot of people out there who have not yet got the message. There are still too many Americans who give the free enterprise system little chance to make it through this decade. But I say the system does work. Give it a chance. I say that initiative and risk taking are still alive and well. Give them a chance. I say that the urge to make it on our own, on our very own terms, is still part of the American dream. Give us that chance. And I say that our ultimate weapon for dealing with the future is an open un-regimented society in which the accidental and unexpected can take root and grow. Give us all that chance. Thank you. (Applause)

QUESTION AND ANSWER PERIOD

CHAIRMAN EDMUND T. PRATT, JR.: Thank you very much, Arthur, for those thoughtful remarks. And once again, after hearing them I'm happy to be able to say that I'm part of small business here in New York. Now ladies and gentlemen, we have with us here two people in positions of outstanding importance to all of us in the business world, and I'm sure there are many questions many of you would like to ask them. We have two people who have been spending a number of weeks trying to get ready to ask those questions for you. Mark Kaplan will be the first questioner followed by Tom Macioce and we'll alternate until we run out of time or out of questions. Mark.

MARK KAPLAN: I'd like to ask Mr. Civiletti a question about a particular kind of small

business. Do you approve of extending the use of undercover agents to detect crime in various branches of the government? And if so, what control should be necessary to prevent abuse or politi...I knew I wouldn't get this word out...politicalization of the process?

BENJAMIN R. CIVILETTI: What was that question? The answer is plain and simple, yes. It's essential today to have undercover operations because crimes that do the most harm in terms of dollars, in terms of injury, direct injury to the public in terms of the corruption or erosion of our faith in democracy or in municipal or local or state or federal government are crimes which don't leave clues, witnesses, great trails of blood, are not observable, are not done at high noon in Times Square. So that they're sophisticated. They're done with the stroke of the pen or through a series of carefully orchestrated meetings or arrangements, at high risk for high dollars. And we have to have inside people, whether they're informants or whether they are undercover operatives, or whether they're in that gray zone between the two, or beyond the two, in sting operations and in the undercover operations. At the same time, there is risk and danger there, and jeopardy to our system of fairness, our perception of justice, and not being trapped – whether you call it legal entrapment or tricked into jeopardizing your career or your reputation or your basic honesty. And those are hard decisions based on facts. The general kind of controls that we have are monitoring, our FBI informant, and undercover guidelines which were first developed by Attorney General Levy. We're about to revise them and tighten them even further. And to make sure that we stay well on the side of what is fair, honest, and make clear to whomever it is who is dealing with an undercover operation, believing it to be criminal, knows up front that he's

dealing with a criminal operation, a criminal organization, someone who is trying to defraud, steal, abuse the system. (Applause)

THOMAS MACIOCE: Mr. Levitt, we have been talking about risk taking and you commented on the subject of capital formation. My question is how can our exchanges, both the American and the New York Stock Exchange become more international financial markets than they are today in view of the fact that extensive pools of capital exist outside of the United States? And as a second part of that question, what steps do you believe can be initiated to attract that foreign capital to our securities markets?

ARTHUR LEVITT, JR.: Well, I think it's a terribly important consideration and there are some factors within the scope of the exchange's abilities to do just that. I think we, together with the SEC, can simplify the process of applying for listing on domestic exchanges. We have alternative listing standards at the present time which make it easier for foreign corporations to do just that. We can also do a more effective job of marketing that process abroad. And the American Stock Exchange, as a matter of fact, has several programs involving taking our companies to Europe and the Far East to show that our marketplace is attractive to international investors. But there are some factors that are beyond our control. The strength of the dollar, the level of confidence in our economy obviously is a terribly important circumstance. But getting back to some of the things that we can do once again, I think the taxing of dividends held by foreign investors, the 30% withholding tax is something that the industry has campaigned against

for a good number of years and still that problem has not been remedied. So I think that should be vigorously pursued. I think it's an important issue and I think it's one that the exchanges are making some progress on and I think it's one that the government is giving very serious thought to at this point.

MARK KAPLAN: Mr. Civiletti, I'd like to turn that question around a little bit and ask whether the government has noticed any material reduction in US asset commitments by foreign institutions as a result of the action taken with respect to the Iranian banks? And what steps, if any, can be taken to reassure the holders, the foreign holders of US assets?

BENJAMIN R. CIVILETTI: The answer to the first question is no, but considerable apprehension and nervousness and the Treasury Department, Secretary Miller and others, have been doing and quite successfully a considerable amount of hand holding and reassuring. Part of the process of avoiding jeopardy circumstances is also some pre-notice and pre-advice and explanation of the limitation and the specific purpose in the Iranian circumstance for the extraordinary exercise of emergency power and the freezing of assets. And specifically not rushing in or suggesting or talking about, in any kind of loose way, a step which I think is an apprehensive step to foreign investors and that's the vesting step.

THOMAS MACIOCE: Mr. Civiletti, in view of the fact that Mr. Levitt has raised the question of the improvement in our balance of trade and the strengthening of our dollar, and given our

national interest in both, improving our balance of trade and the strengthening of our dollar, aren't some of our laws, such as the Foreign Corrupt Practices Act, militating in certain respects against the continuing attainment of that objective? And just how much of a penalty should we be willing and ready to pay just so that we may be able to live with ourselves?

BENJAMIN R. CIVILETTI: The answer to the first part of the question is yes. And the answer to the second part of the question, you'd better be able to live with yourself or it's not very worthwhile, either as an individual or as an institution, or as an entity. Certainly the Foreign Corrupt Practices Act is a restriction, a limitation, a damper on free and unfettered and sometimes even unfairly so in light of foreign practices or foreign customs and the competitors dealing in those practices or customs. But it seems to me that if we hold ourselves out in the United States publicly, individually, as well as institutions, as to deploring corruption, influenced peddling, and bribery, if we become outraged at foreign entities or individuals coming here and engaging in that practice, then we can do no less when we are practicing and trading and marketing in foreign countries. Now the Foreign Corrupt Practices Act is an extremely difficult act to enforce because all the events, occurrences, generally are outside of the compulsory process of evidence and witnesses. So it relies to an enormous extent on the traditional reliance in law enforcement which is voluntary compliance, the basic decency and honesty and wisdom of American citizens, corporate and individual. And in addition to that, we have in the Department of Justice recognized – the SEC has not quite recognized yet – that this is a new adventure, or misadventure in the law – extending the American law extraterritorially which is

very unusual. And therefore, the American public and particularly the business community is entitled to guidance. And we've set up a process, as you know, it may not be perfect and it may not work, but a process for guidance for submissions and reviews and for analysis. And there are certain jeopardies with regard to that but they're not very large. We hope that over a period of some reasonable time, the SEC will join us in that process and that it will become effective and will bring some specificity and some regularity and some cooperation from the government's side to the immense and difficult problems that the corporate side has in this area.

MARK KAPLAN: Mr. Levitt, you discussed your concern for the capital raising processes in the United States. It's been my observation that the number of initial public offerings of securities and public offerings of equity securities has declined markedly over the last decade or so. In your opinion, why has this occurred and what would be necessary to make this source of capital available again, particularly to the smaller corporations?

ARTHUR LEVITT, JR.: Well, fundamentally, maybe simplistically, risk is not being rewarded in America today, where the sum total of capital appreciation and dividend income that could be obtained from buying a security isn't as great as what you could get by buying a corporate or a municipal bond. And we've had a substantial flight from equities. I think there are another two reasons for that. I think that investors have felt that they haven't been able to make money in our equity markets and they're a little bit scared about the system so we've got to restore their confidence. It isn't just confidence in our securities markets although that's part of it. It's kind of

a feeling that the legislature and the administration not only understands the process of business but is willing to do something about it. I think it's a question of considering righting some of the imbalances that have been affected in recent years in terms of the pendulum which swings away from the business community and swings pretty far away from them. And I think that that's got to right itself. It's got to redress itself. I personally believe that our tax laws are a good place to address that issue. I believe that tax incentives such as the reduced capital gains tax of '78 and other sorts of incentives that are being considered at this point are terribly important to reward the risk of undertaking the kinds of commitments that would be involved in bringing the individual back to the marketplace and creating the kind of environment where corporations would find it attractive to sell equities rather than to place themselves in, to sell debt issues. So I think those are the prime characteristics that we need. I think it's both a fundamental question and it's a question in terms of public confidence. And I think we are moving in that direction. The numbers of bills that are floating around the Senate Finance Committee and the House Ways and Means Committee, the statements of the administration with respect to the need for creating incentives for capital formation, and even the kind of grudging statements of the Treasury Department in terms of some of the benefits that came from the '78 capital gains reduction, I think speak to that issue. And I'm very hopeful that we're going to have some substantial progress and that the climate for new issues will improve materially within the next 18 months or so.

THOMAS MACIOCE: Mr. Civiletti, the principle of vicarious liability, and I think you spoke of

your experience in the criminal area, the principle of vicarious liability has been extended to corporate executives such as in the Kroger case where criminal liability was assessed. Do you believe that this principle of vicarious liability should be extended to the point where corporate executives would have to give what amounts to guarantees for each and every act committed by a corporation at whatever level? Or should there be a revision in the criminal code?

BENJAMIN R. CIVILETTI: No, I don't believe that the corporate executive any more than the head of any entity or organization can possibly be responsible criminally and even personally, civilly, for every act which is chargeable to the corporation even though he has, or she has, in a sense authority or supervisory duty and responsibility for all acts of the corporation, in perhaps a civil sense as the head of the corporation. Any more than, although I'm charged with the supervisory responsibility and the duty and the constitutional power and statutory power and all the rest to be responsible for the 55,000 employees of the Department of Justice and every dollar of the \$2.5 billion budget of the department. No top management executive or group of executives can be criminally liable nor personally civilly liable ipso facto for every action of people that are far beyond their knowledge, control, understanding, or even recognition. I think that the Business Roundtable, for example, advocating, and their representatives advocating and discussing and negotiating with the Justice Department and others in the Congress with regard to the criminal code, and vicarious liability or reckless endangerment or whatever phrase or catch-phrases that you want to apply to it, have come to a reasonable compromise. Sure, I could develop on the government side, spectres of enormously bad conduct for which culpable parties could be excused under that formulation. On the other side, corporate executives and good

lawyers could stay awake nights hypothesizing on what the government could do under that formulation. But I think generally a good balance has been struck, and among other things, Ed and I were discussing that very subject tonight. And I said that within the Department of Justice, there's been a growing development not only to respond positively and in a reasonable, and I hope logical way during the terms of office of Attorney General Levy and Judge Bell and to some extent myself, but to try to institutionalize that kind of response and policy of how the government intends to operate through written standards, written guidelines, written regulations, which at the same time inform and set a pattern of conduct within the law by the government particularly in areas as sensitive as this area and the prior area that you mentioned, the Federal Foreign Corrupt Practices Act.

MARK KAPLAN: I'd like to keep you up there, if I may, with a question slightly offshore. And that is, can anything be done legally or otherwise to prevent foreign governments from using our traditional willingness to accept refugees as a device for their own political purposes and to embarrass the United States?

BENJAMIN R. CIVILETTI: I need a little help on that. I guess there are three answers to that. One is that through the general foreign relations and the give and take of foreign relations we can make it so disadvantageous to a government to, or try to with the help of our allies and other nations that have a common interest to prevent dumping, the inhumanity of dumping citizens into the sea or across borders, to make the disadvantages greater than the advantage achieved

through political embarrassment, removing segments of the population, undesirables, political opponents, or whatever it happens to be. And we have to do that. That's number one. Secondly, I think that in a harsher sense perhaps we have gotten to a point in the immigration law which was recognized some years ago as developing and when the president established the Select Commission on Immigration and Refugee Policy, he fully recognized it a year ago, where we have tied ourselves up so much in the intricacies of the law that we are unable to meet the principal objectives and achievements which are essential to any nation, and particularly to Americans, to determine who comes to the United States and who is accepted under the law and who doesn't. And I think that requires a revision and that's what the Select Commission is working on – an in-depth, comprehensive revision of the immigration and refugee law as well as, and a strong, concomitant part of it, a very vital, energized enforcement policy including the Coast Guard as well as the Border Patrol, Land and Sea and Air.

THOMAS MACIOCE: Mr. Levitt, we have seen recently an increase in proposals to mandate structured memberships on corporate boards by governmental action and suggestion. We've also seen suggestions made for the elimination of legal counsel from corporate boards. My question is two-fold. Do you agree, as far as it affects firms of the size listed on the American Stock Exchange, with the program to eliminate company counsel from corporate boards? And do you favor the appointment of representative members on the board affiliated with particular groups such as employees, consumers, environmental, or other particular special interest groups?

ARTHUR LEVITT, JR.: Well, the problems of the smaller companies listed on our exchange are somewhat different than the larger, traditional companies both in terms of attracting directors and in terms of the kinds of specialized needs that those companies have. It's more expensive for us, for our companies to attract those directors and somewhat more difficult. And furthermore, I think that to mandate the structuring of a board which becomes a matter of considerable importance in terms of the direction of the company and in terms of what the company's objectives may be, is something that I'm uncomfortable with, either in terms of whether it be an environmentalist or a representative of a community group, or even the prohibition of company counsel from service on that board or being part of the board's structure. The SEC recently asked that both exchanges make, as a condition of listing the imposition of an Audit Committee with outside directors as part of the process. The New York Exchange has that as a condition of their listing and we chose not to. We asked the SEC for the right to try over a period of time to persuade our companies to implement Audit Committees because we felt that most of them already had them. And indeed, the response to our request has been very encouraging and I think well over 85% of our companies now have Audit Committees with outside directors on them. So I think this is a process that the companies must come at on their own. It's a process of evolution and I have a lot of reservations about a mandated board of any kind, any shape, any form.

MARK KAPLAN: Mr. Civiletti, it is sometimes discouraging to find several US agencies or federally-funded organizations on opposite sides in time-consuming and expensive litigation. Can or should something be done at a policymaking level to reduce or eliminate these conflicts?

BENJAMIN R. CIVILETTI: Yes, and it's a growing, it's a growing problem. The Department of Justice fights tooth and nail, tooth and nail, to preserve litigating authority for just that purpose. So that we don't get into litigative circumstances, either administrative litigation or court litigation wherein we have these independent agencies or departments or semi-independent departments in court saying one thing on a principle of law and another saying another thing. And consistently, agencies reform proposals, congressional committees with their particular department or agency in which they have a relationship, where there's authority, oversight, and power, will try to enhance the stature and ability and the independence of that particular department or agency by trying to mandate through legislation independent litigating authority. And they've been successful in any number of areas. We oppose them all. We oppose them on the floor. We oppose them in the committee. We oppose them by serial references back to our committees, in effect the Judiciary Committees of the House and the Senate, because we think they're tragic. They're nonsensical, they're costly, they confuse the law. And they abuse the public, both individuals and the business public. But they're hard fights, and very seldom do we see members of the public of any kind coming up watch-dogging that kind of separatism or that kind of division. We don't mind, and have no objection, to carefully considering the views of different agencies if it's, for instance, a recent dispute arose between the Department of Labor and the Department of Transportation. We don't have any role in policy in transportation. That's in the Secretary of Transportation. Nor in labor, that's in the Secretary of Labor under the president's guidance and direction. And we have no hesitancy in listening carefully on litigator

decisions to the judgments of each of them and making the call as to which way to go in a particular suit based on the facts and the law. And we have no objection to entering into a memorandum of understandings with the departments, any department, so that they can share in the participatory activities of litigation so long as the authority and the control and the disposition of important decisions are left to one authority, the Attorney General, or the Solicitor General in the case of the Supreme Court and appellate cases, so that there's uniformity, there's a point of view, and you don't have the ridiculous circumstance of two or three different federal agencies and departments either battling each other or inconsistently battling a particular line of commerce or industry.

CHAIRMAN EDMUND T. PRATT, JR.: Might we have one more question from each, please.

THOMAS MACIOCE: Mr. Civiletti, let me ask you a question. Given the alleged limited resources of the Antitrust Division of the Attorney General's Office, should it be extending its activities to the speculative expansion of the law such as the shared monopoly cases? Isn't the pursuit of those cases an expansion of the antitrust laws beyond what Congress had in mind? And in an industry where there may be four or five major producers, isn't the pursuit of such cases and investigations a substitution of centralized planning for the operation of the free market?

BENJAMIN R. CIVILETTI: I don't know many of the answers to that multi-face question. I've

heard it said that some antitrust lawyers are just delighted that we've been fooling around for three years in shared monopolies. It's kept us busy without doing any real harm. (Laughter)

Certainly the Antitrust Division has more resources than they need right now. They're the largest division, litigating division, in the Department of Justice. They have the highest average cost per employee within the Department of Justice. I know the work is difficult. I know it's very sophisticated. I know you need experts and economists and all the rest. But some people suggest that we get less bang for the dollar out of the Antitrust Division than any other division. So it's not a question of having precious and limited resources which are being abused by looking at shared monopolies. And the shared monopoly mystique to me is overstated. I think it's old wine in new bottles. I think the principles underlying shared monopolies are not substantially different than the common Sherman Act principles at all in any way. And I think that the survey, in fact, of originally 400 companies in different lines of commerce, then revised down to 75 for a closer view, and then revised again to less than 15, has shown, and in a way been quite beneficial, and has shown that there are not illegal, anti-competitive prices going on in lines of commerce and between companies in areas where there appear to be something wrong or you could argue there's something wrong. It's proved out overall, I think, overwhelmingly that competition is alive and well. It's been survival of the fittest, healthy, and that we don't have a lot of anti-competitive, illegal conduct going on. We are still reviewing, Sandy Litvack is reviewing I guess less than those 15 cases, maybe less than 10 cases, and there may be within that small percentage, some which merit some action. I don't know yet. I will not be disappointed, myself, if there are no cases that finally develop. I think it was worthwhile and I think it was within the

tradition of standard law, a slightly different perhaps drawing of inferences, but not revolutionary, not beyond legislative mandates, and certainly not dangerous generally to the community.

MARK KAPLAN: Mr. Levitt, after that discussion of the antitrust law, I'm also embarrassed to ask you the next question. But we've read a lot about the potential merger of the American Stock Exchange and the New York Stock Exchange, would you like to comment on that particular antitrust problem? (Laughter)

ARTHUR LEVITT, JR.: I think it's unlikely. (Applause)

CHAIRMAN EDMUND T. PRATT, JR.: Benjamin Civiletti and Arthur Levitt, Jr., to both of you, our most sincere thanks for taking the obvious time to prepare thoughtful comments for us and for your candor and interesting answers to our questions. As Mr. Levitt pointed out, New York is in many ways a town of small businesses, but we are still the Big Apple. And one of the traditions of our Club is to present to our speakers, as a small souvenir of the evening, if I can get it open here, a Steuben Big Apple. (Applause) Take it with our thanks for you have enriched and instructed us this evening and we appreciate you're being here. Members and guests also, thank you for coming. Goodnight.