U.S. SENATE COMMITTEE ON

Finance

SENATOR CHUCK GRASSLEY, OF IOWA - CHAIRMAN

http://finance.senate.gov

M E M O R A N D U M

To: Reporters and Editors
Re: SEC "global settlement" case
Da: Monday, April 21, 2003

Sen. Chuck Grassley, chairman of the Committee on Finance, along with key colleagues, has been corresponding with the Securities and Exchange Commission (SEC) over the $1.4 billion global settlement the SEC has reached in principle with Wall Street's largest firms over allegations of conflicted stock research. Grassley's concerns are twofold: whether the SEC is taking into account that the firms might be able to deduct part of the settlement's cost from their taxes, at the cost of other taxpayers, or have insurers pick up the tab; and whether the SEC will disclose the terms of the settlement to the public before voting to approve the settlement. Grassley's staff learned today that the SEC has no plans to release the settlement details to senators or the public prior to the vote, which could come as early as this week. Grassley made the following comment on that development.

"I'm worried that the SEC is deciding to operate in the shadows instead of the sunlight. The SEC appears set to ignore the bipartisan request for full disclosure of the $1.4 billion agreement with Wall Street prior to the SEC vote. If it's a good deal for taxpayers and investors, then it should be able to withstand public scrutiny prior to the vote. We should all know the tax and insurance consequences of this proposal. Operating in the dark only heightens my concerns that Wall Street may be getting just a slap on the wrist."

The original letter Grassley co-wrote to the SEC follows.

February 28, 2003

The Honorable William H. Donaldson
Chairman
Securities and Exchange Commission
450 5th St. NW
Washington, D.C. 20549

Dear Chairman Donaldson:

We are writing to you regarding the Securities and Exchange Commission's (SEC) review and approval of the settlement of lawsuits against certain Wall Street firms. These settlements resolve claims of stock research abuses.

We are very concerned about press reports that these settlements are being structured to maximize the amount of the payments that are tax deductible, thereby leaving the American taxpayer to pick up much of the tab. In addition, we question the wisdom of settlements that have been carefully structured to allow investment bankers and Wall Street firms to pass the bill on to their insurers.

This is unacceptable. Congress has pressed hard for real change at the SEC and in the boardroom. We are not interested in settlements that look good in the newspaper headlines but fail to bring real accountability. It is disingenuous to hold press conferences highlighting settlements which fail to mention that a significant portion of the payments may be deductible and are covered by insurance.

It is particularly galling that as American families sit at the kitchen table filling out their tax return and pay their fair share to the U.S. Treasury, SEC spokeswoman Christi Harlan stated in response to concerns about the tax treatment of the settlements with Wall Street: "The SEC enforcement staff looks at violations of securities law; we don't take other factors into consideration."

The SEC may not take into consideration the tax treatment of settlement payments or who ultimately makes such payments. Let us assure you, though, that we are concerned and we expect the SEC to reconsider its apparent apathy about the tax treatment of settlements and who is liable for making such payments. Accordingly, we request that as part of the SEC's consideration of these settlements that all Commissioners are provided a general analysis of the tax treatment of these settlements – specifically, what portion will be deductible and what deductibility will mean generally for the firm in regards to tax savings as well as in terms of potential loss of revenue to the Treasury. In addition, we request that the Commissioners be advised as to what portion of the settlements will be payable by the settling firms' insurers and what such payments will mean for each settling firm.

That said, we recognize that payments of restitution are deductible and believe the tax code should not penalize efforts of direct restitution. However, we are concerned that payments may be presented as restitution for tax and other purposes but will not translate into real relief for those harmed.

For the SEC to be oblivious to the tax treatment and the ultimate payor of a settlement is to have the SEC working contrary to other functions and goals of the U.S. government. In addition, the SEC and states' attorneys general are naive if they do not believe that the tax treatment is of great importance to the Wall Street firms. As the Finance Committee continues its review of the tax treatment of fines and penalties it is with an eye toward the reality that lawyers with sharp pencils can always try to find a loophole. It is essential therefore that the SEC and states' attorneys general not act as an indifferent or unwitting partner in firms attempts to minimize their settlement costs through the tax code. While the SEC has its own resources, if you have any questions about possible tax treatment of a settlement, we encourage you to seek guidance from the Treasury Department.

We ask that you make available to us the same analyses provided to the Commissioners regarding the general tax treatment of the settlement and whether or not these costs will be borne by insurers of the firm at question. Bottom line: the Commissioners and the American taxpayer need to know how much each firm will pay that will not be deductible and will not be paid by an insurer or other third party.

There have been words about the need for change and reform both at the SEC and in Corporate America. Now is the opportunity to show the American people with action that makes those responsible bear the full burden. However, artfully crafted settlements of corporate wrongdoing that have the taxpayers subsidize this wrongdoing or have the costs paid for by somebody else will only convince us that words are still all there is. We appreciate your prompt response to this matter by March 10, 2003.

Cordially yours,

Charles E. Grassley
Chairman

John McCain
Chairman

Max Baucus
Ranking Member