ADDRESS

of

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It is a great pleasure for me to be in Chicago again and to have the opportunity to discuss with you the program for revision of rules and regulations under the new administration of the Securities and Exchange Commission. When I received your kind invitation, it occurred to me that in speaking before your group of highly competent working secretaries of corporations subject to the requirements of the Securities Exchange Act of 1934, I would be justified in discussing in some technical detail a number of the revisions of rules and regulations pertaining to such corporations which the newly constituted Commission has put into effect or has under study and consideration. I will also mention, but not discuss in detail, revisions pertaining to securities dealers and brokers and certain other aspects of our rule revision program.

First, however, let me paint with a broad brush stroke a few general word pictures of the Commission at the end of its first six months under the Eisenhower Administration.

As you know, the five member Commission is required by law to have no more than three of one political party. Now is the first time since the Commission was established in 1934 that there have been three Republican members. However, one of the three new members appointed by President Eisenhower is a member of the Democratic Party and I think it is a fair statement that the five Commissioners, the new and the old, have been working together harmoniously toward common objectives. You will recall that the report of the Hoover Commission's Task Force found that the Commission "on the whole has been notably well administered," that the critics of the Commission "concede that its staff is able and conscientious, and that the Commission generally conducts its work with dispatch and expedition where speed is most essential." It also said: "There are of course some weaknesses . . . but in evaluating them, one should keep in mind the basic fact that the Commission is an outstanding example of the independent commission at its best." I can assure you that my personal observation of the Commission, as presently constituted, and the vast majority of the Commission staff bears out this reputation for high professional service by men dedicated to the public interest.

When we went to work last July, we inaugurated a broad program of study of the rules, regulations and forms which have grown up at the Commission over a period of twenty years. Our objective was to simplify, streamline and speed up the orderly administration of the statutes committed to our charge. We were impelled to this revision program not only out of a desire to clean out a lot of dead underbrush in the forest of regulation for the purpose of facilitating the free flow of investment capital into American enterprise, but also because we believed that the basic investor protections afforded the American public by these laws could be strengthened and enhanced by a more realistic, practical and vigorous administration of them.

I emphasize the dedication of the present Commission to the philosophy of the laws we administer. The public interest, the protection of investors and, under the Holding Company Act, the protection of consumers, are our statutory objectives. Some individuals, writers and legal authorities from time to time may attack the new Commission or question its dedication to the objectives of investor protection. Theodore Roosevelt said "Walk softly but carry a big stick" so I hesitate to emphasize the point further by speaking, but I must leave in your minds the impression that this Commission is engaged in as vigorous an enforcement of the federal securities laws as our legal powers and personal capabilities permit.

Now let me turn to some of the things we have done or are in the process of doing in the area of rule and form revision since last July.

We have adopted a new accounting rule dealing with stock options.1/ The Commission decided against prescribing any particular procedure for determining the amount of cost, if any, of stock options to be reflected in profit and loss or income statements. However, in order that investors may be informed of the dollar significance of stock options granted to officers and employees, the new rule requires full disclosure of all stock option arrangements in financial statements filed with the Commission.

We have eliminated the requirement of filing of quarterly reports of gross sales and operating revenue. Because of short term and seasonal business changes and the frequent occurrence of a net earnings trend contrary to the gross trend in a company, these 9-K reports were abolished.2/

We have revised the proxy rules under the Securities Exchange Act of 1934. I will discuss later some general problems affecting the Commission in this action, but right now let me talk of the revision itself. Many of the changes made are of a clarifying nature. It has been made clear that state law is the standard for determining what is a proper subject for action by security holders in connection with security holders' proposals. It is now specifically provided that management may omit from its proxy material a security holder's proposal which relates to the conduct of the ordinary business operations of the issuer. A new provision has been adopted to relieve management of the necessity for continuously repeating in its proxy material security holder proposals which have received little security holder support. Under the amended rules, a security holder's proposal may be omitted from management's proxy material if it was submitted within the previous

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1/ Securities Exchange Act Release No. 4958.

2/ Securities Exchange Act Release No. 4949.

five years and received less than 3% in the case of a single submission, less than 6% upon a second submission or less than 10% upon a third or subsequent submission during such five year period. Also, the new rule requires data about all the directors even though, because of staggered terms, less than all are standing for election.3/

We are considering a proposal to revise the annual reporting forms under the Securities Exchange Act of 1934. A principal purpose of the proposed revision of Form 10-K is to conform its requirements, so far as is practicable, with the corresponding requirements of Schedule 14A of the proxy rules and to provide for the substitution of proxy statements filed under those rules for most of the information required by the items of Form 10-K. In addition, the proposed revision would permit financial statements contained in the proxy statements, or in accompanying annual reports to security holders, to be incorporated by reference in satisfaction or partial satisfaction where such statements substantially meet the requirements of that form.

Thus a major effect of the proposed revision will be to eliminate filing of information already reported in the proxy statement.

The proposed new form, in addition to simplifying the reporting requirements, also provides that companies which file reports with the Federal Power Commission may substitute their reports to that Commission for the information items and, subject to certain conditions, for the financial statements, required by Form 10-K.4/

We are also considering a proposed revision of the current report form, Form 8-K, which would limit the requirements of the form to matters of such material importance to security holders as require a report on a current basis.5/

We have just adopted rules under the Securities Act, and complementary rules under the Holding Company Act, which will eliminate the delay in offering of securities to be offered at competitive bidding and will dispense with the necessity of obtaining routine supplemental orders previously required. Under these rules, the post-effective amendment to the registration statement will become effective automatically on filing in one of our regional or branch office and no supplementary order under Rule U-50 is required if two or more bids have been made for the securities.6/

3/ Securities Exchange Act Release No. 4979.

4/ Securities Exchange Act Release No. 4961-X.

5/ Securities Exchange Act Release No. 4961-Y.

6/ Securities Act Release No. 3494; Holding Company Act Release 12298.

We are also considering a proposed simplification of the so-called "when issued" trading rules which will eliminate 14 rules and 2 forms. The only cases in which Regulation X-12D3, Registration of unissued securities for "When Issued" Dealing, still serves a practical purpose is where the securities to be traded are the subject of a voluntary subscription or exchange right granted to the holders of a security traded on an exchange. The proposal contemplates that Rule X-12A-5, Temporary Exemption of Substituted or Additional Securities, be amended to cover these cases and generally simplified. Rule X-12A-5, which is applicable whether the new security is issued or unissued, should be far less burdensome to issuers and exchanges than Regulation X-12D3, and in almost all cases public information concerning the transactions is available either under one of the Acts administered by the Commission or otherwise.7/

We are considering simplified rules and application forms in connection with listing additional amounts of outstanding securities on an exchange. Under the existing practice, registration of a security on an exchange under Section 12 of the Securities Exchange Act is effective only as to a specified number of shares or a specified amount of a class of security so that if additional shares or amounts of the same class are subsequently issued, a new application on Form 8-A must be filed for registration of the additional amounts. Under the proposed revision, the original application for registration would be deemed to apply for registration of the entire class, and the registration of unissued shares or amounts would become automatically effective when they are issued, without further application, certification or order.

The matters I've just discussed have been put out for public comment or actually adopted. Now let me mention a few that are in the mill but not yet actually released.

We are considering revision of the numerous forms used by officers, directors and others for reporting the ownership or changes in ownership of securities of companies subject to the Securities Exchange Act, the Holding Company Act and the Investment Company Act. It will be proposed that the seven forms now used for these purposes be simplified and consolidated into two or three forms. In this connection the Commission is also reviewing the reporting forms and rules under Section 16 of the Securities Exchange Act which we think are needlessly complicated and hard to understand. These are the forms and rules relating to insider trading, you will recall.

We are studying the form for registration of employee stock offerings with a view to expanding its use. The present Form S-8 is

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7/ Securities Exchange Act Release No. 4969-X.

very simple. It provides wide latitude for the use of the issuer's annual report to security holders and other published material readily available. The Commission has directed the staff to study the possibilities of amending the rules for the use of the Form to permit use of the Form by a larger number and more varied types of employee stock offerings. It has also been suggested that the Form, as revised, might be made available for offerings under employee stock option plans.

The staff also has under consideration a simple Form which would be available for registration of offerings of institutional grade debt securities. It is hoped that such a form will make possible faster, simpler and less expensive registrations of such debt issues, on a basis more nearly competitive with private placements. We contemplate using our acceleration power under Section 8(a) of the Securities Act to permit such issues to be registered more quickly than is presently the practice.

The revisions I have just discussed in some detail are those I think you may be most interested in as secretaries of corporations registered under the Securities Exchange Act, but to round out the picture of what we have been doing since last July and contemplate for the next few months, just let me list a few others:

We have adopted new forms for registration of management investment companies and for registration of securities of open end investment companies, new rules concerning registration and reporting requirements for investment companies,8/ and a new rule requiring brokers and dealers to file financial statements with their applications for registration,9/ and have released for comment a proposal for a 9-item form for registration of securities brokers and dealers instead of the present 27-item form,10/ and adopted simplified forms and reports of brokers and dealers associations to eliminate voluminous exhibits containing information otherwise readily available.11/

We have adopted a rule relieving exchanges on which a security is admitted to unlisted trading privileges from reporting information which duplicates information reported by the issuer where the security is fully listed on another exchange.12/

8/ Investment Company Act Releases Nos. 1932 and 1933.

9/ Securities Exchange Act Release No. 4973-X.

10/ Securities Exchange Act Release No. 4973-X.

11/ Securities Exchange Act Release No. 4942.

12/ Securities Exchange Act Release No. 4914.

We have put out for comment a proposed rule to exempt from competitive bidding issues of state regulated utility subsidiaries of holding companies, where the issuance of such securities is entitled to exemption from the Public Utility Holding Company Act of 1935, thus breathing life into Section 6(b) of that Act which, up to now, has been for all practical purposes ignored,13/ and also a proposed simplified rule, designed to supplant the present complex rule, relating to permitted financial connections of officers and directors of companies in holding company systems.14/ A revised annual reporting form for service companies in holding company systems has been adopted.15/

We have adopted a new rule prohibiting trading in unvalidated German bonds.16/

We are presently studying and hope to circulate for comment within the next several months a revised registration form for securities of closed end investment companies, new registration forms and rules for investment advisers, a form for financial statements of brokers and dealers, a revised system annual reporting form for utility holding companies, revised quarterly and annual report forms for management investment companies, and rules to regulate stabilization of the price of securities being publicly offered.

So much for the rule and form revision program. Now I want to spend a little more time with you visiting the new revision of the proxy rules which, as you all undoubtedly know, was promulgated on January 6. It is in connection with the proxy rules that serious, and I submit unfounded, charges of lack of interest in protecting the investor have been made against the new administration of the Commission. Representatives of independent stockholders, scholars and others who appeared before us at the hearing on December 16, 1953, charged that the new proxy rules will have the effect of thwarting and strangling corporate democracy. I submit that the Commission has no such purpose and I submit that the new rules will have no such effect.

Let me mention a few of the basic problems involved. One of the phenomena of the early days of the New Deal was the emergence, not only in America but abroad, of great personal Leaders. This was attended here by surrender of broad legislative powers by Congress to the Executive Branch of the Government.

13/ Holding Company Act Release No. 12217-X.

14/ Holding Company Act Release No. 12242-X.

15/ Holding Company Act Release No. 12287.

16/ Securities Exchange Act Release No. 4983.

In its examination of its legal powers, the new Commission has been staggered by the tremendous areas in which it possesses power of a legislative character. Many, many times the statutes give the Commission unlimited blank checks to make rules and regulations. Section 14 of the Securities Exchange Act of 1934 is an example. It makes it unlawful to use the mails or instrumentalities of interstate commerce to solicit proxies in respect of securities registered on any national securities exchange and, I now quote, "in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors." Although abuses by corporations of the proxy soliciting mechanism were specifically referred to, the Committee Reports and other guides to legislative intent give the Commission little help in precisely determining what kind of rules and regulations the Congress had in mind that the Commission should adopt in this field.

The proxy rules have been amended half a dozen times since the first hesitant approach was made in 1936. But not until December of 1942 did the Commission first adopt the shareholder proposal rule. I think the Commission's purpose was at first misunderstood in the 1942 revision as it was feared that the Commission was attempting to minimize the rights of minority shareholders, and bills were introduced in Congress to limit the Commission's power in this area. The then Chairman of the Commission, in hearings in June of 1943 before a Subcommittee of the Committee on Interstate and Foreign Commerce of the House of Representatives, testified in defense of the rules and no bill was enacted.

An industry representative at the hearing before the present Commission on December 16, 1953, argued that the Commission had lulled the Congress to sleep in promulgating the rule after the session adjourned in 1942, but it seems to me that the failure of enactment of a bill limiting the Commission's power, and the subsequent election of five Congresses without amendment of Section 14 of the Act, should be considered in this connection. In any event, the then Commission assured the Congressional Subcommittee that the proxy rules would be beneficial to minority shareholders and, indeed, to shareholders generally, and that the Commission in its administration of the rules would see to it that they were not abused.

I deny that in the new revision of the proxy rules we are strangling corporate democracy, as our critics say. I would like to call your attention to what democracy means. Since ancient Athens democracy has meant some form of government by majority rule. Democracy, however, is not inconsistent with a form of government in which the majority speaks through chosen representatives. The history of governmental organizations in America, and indeed the history of the development of corporate organizations, bears out this thesis. In American political democracy, the people speak through their representatives in the state legislatures and in the Congress. But the "initiative"

or legislative proposal initiated by the people directly rather than by the legislature, thought by its proponents in the last half of the nineteenth century to be the ultimate improvement in political democratic methods, has proved virtually useless in the states which have tried it. In corporate democracy, the people act through their directors whom they, as shareholders, elect. The ultimate and truly democratic recourse of the shareholder against a management unsatisfactory to him is to unseat the Board of Directors, and you are undoubtedly familiar with the many successful proxy fights that have been waged by dissatisfied shareholders under the proxy rules administered by the Securities and Exchange Commission.

In considering the shareholder proposal rule in the light of this concept of democracy, we then turn to the question of reasonable administration of the rule for the best interests of the majority of the shareholders against the continuing dissident harassment of a few. In ten years of the shareholder proposal rule, only 181 shareholders out of the millions of American shareholders of registered companies have submitted proposals, none have carried and the vast preponderance have been voted down by overwhelming vote of the shareholders voting. It's about time for the preachers of corporate democracy to remember that corporate democracy means rule by the majority of shareholders.

In political organizations, candidates for public office are often required to supply a specified number of signatures in order to get on the ballot. We recently saw the spectacle of the Mayor of the world's largest city -- New York -- ineligible to run for reelection because an insufficient number of citizens signed his nominating petition.

President Eisenhower expressed in his State of the Union message a year ago "dedication to the well being of all our citizens" and emphasized in his speech to the nation a week ago that this Administration's program is "inspired by zeal for the common good." Applying that to the securities law standard we are sworn to support -- namely the public interest and protection of investors -- I think that means the general public interest and the protection of investors generally in the administration of our admittedly broad power under Section 14 of the Act.

The Commission and its staff are familiar with shareholder proposals since 1943. We have concluded that shareholders generally are entitled, in the true sense of corporate democracy, to require a minimal showing of shareholder acceptability and continued progress as conditions of continued resubmission of shareholder proposals in management proxy soliciting material.

You may be interested in knowing that a proposal for a five and ten percent step-up initiated within the Commission was considered as long ago as November of 1951. The new Commission, indeed, cannot claim a copyright on the idea of the progressive percentage increases embodied in the new proxy rule.

Let me mention before I leave the proxy rules a few other related matters. Opponents of the new rule severely criticized the clarification which we hope it makes in the frame of reference for the admissibility of certain types of shareholder proposals to the law of the state of incorporation. This reference to state law is entirely consistent with the previous proxy rules and, indeed, is the only frame of reference, in the absence of any direction from Section 14 of the Securities Exchange Act, that is possible. I submit that it is in complete harmony with the decision in the so-called Transamerica case.17/ As I read that decision, the court found affirmative authority under Delaware law for submission of one of the three proposals and no lack of authority for the two others and simply struck down a corporate by-law which would have placed a procedural block in the way of their consideration by the shareholders. The new proxy rule, I submit, is in entire accord with the legal bases of that decision and consistent with the court's statement that "a corporation is run for the benefit of its stockholders and not for that of its managers." I also call your attention to the fact that the former Associate General Counsel of the Commission, now Professor of Law at the Harvard Law School, Louis Loss, has written in his authoritative treatise: "Where the state law is clear that a particular matter is for the directors alone, that would seem to be decisive; if Congress had intended to give the Commission power to re-allocate functions between the two corporate organs, so revolutionary a federal intervention would presumably have been more clearly expressed. This would approach federal incorporation in all but name. As we have seen, federal incorporation proposals have recurrently appeared in Congress." Let me add, not enacted.

In saying these things about the revision of the proxy rules to you, I want to make it perfectly clear -- and I welcome the chance to say this directly to a chapter of the Corporate Secretaries -- that the revision is not intended to be responsive to some of the arguments presented by representatives of your Society or of certain large corporations who appeared before us at the hearing on December 16, 1953. These representatives made some arguments that you may want to do some further thinking about as the coming year rolls on. Also, I question whether all of the data that could be gotten together has been presented to us. For example, the argument was made that shareholders submitting proposals should defray the cost of their submission in certain cases, but in response to a question from the Chairman of the Commission as to

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17/ SEC v. Transamerica Corp., 163 F. (2d) 511.

the cost to corporations of shareholders' proposals, it was stated that no attempt to compile such costs had been made. I think from your standpoint this argument might lead to the suggestion that management should defray the cost of management proxy soliciting material by which management gets elected to office year by year, and I wonder how seriously your organization would back the argument that a corporation should not pay whatever cost there is in including shareholder proposals in the management proxy soliciting material.

The argument was made before us that "the security holder has a basic weapon to defend his independence which the citizens of the most ideal democracy do not possess, namely, he can express his disapproval of a company's policy by severing his connection with it." In other words, if a shareholder doesn't like the way a company is being managed, he can sell his shares. I doubt very much if the financial officers of companies which have had to go into the market to raise equity capital or which, because of the need to retain earnings in their businesses for use as equity capital, have been interested in seeing that the market values of the shares were well preserved, would feel very happy about this argument and I am sure this viewpoint does not represent the views of the vast majority of American management.

I have taken enough of your time. I will stop now and will try to answer any questions you may care to submit. And I thank you very sincerely for the opportunity to tell you what the new Commission has been doing and plans for the immediate future in the field of rules and forms under the various Acts we administer.