

For Release on Delivery

ADDRESS

of

Robert K. McConnaughey,

Commissioner, Securities and Exchange Commission

before the

PITTSBURGH SECURITY TRADERS ASSOCIATION

Shannopin Country Club

Friday, May 2, 1947

It is somewhat more than six months since I first had the privilege of speaking to a group of the Security Traders. That was at a delightful luncheon in San Francisco last September. Some of you who are here this evening were present then. It is good to meet with you again here in Pittsburgh, and to talk again with you, and with your Pittsburgh colleagues, about some of the problems in which you, as members of the securities industry, and we on the Commission, have a common interest.

I don't propose to announce any startling new policies of the Commission tonight. Nor do I plan to discuss in any detail the technical aspects of questions we have had under consideration. This doesn't seem to me to be the sort of occasion for that.

Instead I want to speak further, and rather briefly, about the subject that bore the main burden of my remarks in San Francisco -- about the desirability of a closer understanding between members of the securities industry and the Commission -- and continued collaboration by representatives of the industry with the Commission and its staff in attempting to work out practical ways of dealing with the problems we have in common.

Although there had been much private discussion about the desirability of such collaboration I don't recall that recently it had been publicly urged on the Commission's behalf until last summer and early fall.

Since that time there has been a highly gratifying conversion of what might have been merely a pleasant exchange of benign sentiment into practical work together.

In San Francisco I pointed out that the SEC came into being at about the same time as the National Security Traders Association. I said that we are concerned officially with many of the same problems that concern you in your day to day business -- that we are concerned basically, as you are, that

the securities markets shall function efficiently -- that we are concerned, as you are, that those markets shall serve with the highest effectiveness in the gathering of capital, genuinely needed to finance industrial and commercial enterprise, and in providing facilities for the ready exchange of interests in such enterprise between those who want to dispose of them and others who want to acquire them.

There is no point in discussing here the economic justification of the distribution and trading of securities. I think we would all agree that those functions are not only useful but essential to the effective operation of our system of enterprise. It is one of our main interests on the Commission to see to it that those functions continue to be performed efficiently. It is a principal objective of our authorities to see to it that the market for securities is kept free from rackets and that consequently public confidence in the markets is maintained. It is a part of that responsibility to see to it, as far as practical within our statutory powers, that the distribution and marketing functions are so conducted as to be free from fraud and manipulation and that all participants have access to the information they need to have to make sensible decisions.

I suggested last September in San Francisco that the concern we have with these matters as public officials is no more direct and no more positive than the concern you have with them as members of the industry if you expect to continue, year in and year out, to make your living through the distribution or trading of securities.

I mentioned then that within the securities industry the view is still widely accepted that the interests and objectives of the Commission are antagonistic to the interests and objectives of the members of the industry. I said that the persistence of that attitude has in the past impeded our working

together as fully as we might to make practical improvements in our rules and procedures, and in your operations, that might well reduce the burdens of regulation that now fall upon you and diminish in many details the complexity of the machinery we now operate in an effort to achieve effective restraints upon malpractice in your business.

The cooperation we have received since last September has been highly gratifying. A great deal has happened since then. I hope that more will happen in the future, with similar cooperation. If we continue to get that kind of cooperation, ultimately our job should be much easier and more effective. More important to you, we should be able to cut to a minimum those practices in the securities industry which are bad for your customers and bad for your business without laying upon legitimate operations as heavy a hand as still remains necessary in some instances to keep effective restraints upon your malefactors.

Since last September we have substantially simplified some of the major forms and procedures to be used in registering securities for public distribution. The approval of the revised forms and procedures brought to fruition a project commenced long before. It had required meticulously careful study. In working out those changes we had the benefit of innumerable helpful suggestions from many people in the securities business. Those suggestions contributed substantially, to an extent that is difficult fully to evaluate, towards what is proving already to be a most helpful result.

I am convinced that the registration forms and procedures have not yet achieved, by any means, the ultimate degree of simplification and practicality that can be achieved. The present forms and procedures seem to be working as a great improvement over those previously used. But we have no disposition to regard the job as finished. The Commission and its staff learns constantly through its experience with the actual use of those forms and procedures.

They will continue to be simplified and improved as rapidly as it is possible to evaluate clearly the specific possibilities for simplification and improvement. I hope that you in the business will continue to criticize what appear to you to be defects in them and to suggest what appear to you to be desirable changes. I assure you that those criticisms and suggestions will be welcomed and will receive careful, objective consideration. They will be tested against the requirements of the Act and against the experience of the Commission and its staff, gained through their efforts to make the Act effective. They will be incorporated into our procedures and forms if they prove to be practicable and consistent with the purposes of the legislation under which we operate.

Since last fall we have attempted also, through encouraging wider use of red herring prospectuses, to develop improved methods of getting adequate, accurate information about proposed security issues broadcast in advance to those engaged in public distributions. In working out these changes, too, we had the benefit of consultation and suggestions from many representatives of the securities business. Those suggestions were infinitely helpful in appraising the problem, in matching the advantages and disadvantages of numerous proposals, and in working out the procedures finally agreed upon.

Here too we are not satisfied that we have reached the ultimate degree of effectiveness. Indeed there are some readily apparent defects in the current operation of the revised procedures. Some of the difficulties doubtless derive from their novelty. These will shake down with time and experience. Others may prove to be fundamental difficulties that will require further changes, perhaps drastic ones. We shall welcome your criticisms and comments with respect to all of this. They can be extremely helpful. One of the other projects --- (and perhaps the major one) --- that has come into public consideration since last September has been our undertaking to review the

Securities Act of 1933 and the Exchange Act of 1934 to discover whether changes are needed in those Acts and if so what changes.

In undertaking this extremely difficult and complicated analysis the Commission publicly invited suggestions from the securities industry, from representatives of those who issue securities, and those who buy them, and from other groups who have a reasonably direct interest in the operation of these two Acts.

The responses we have had to these invitations has been a source of great assistance to us. There has been great diversity in detail in the criticism of existing provisions we have received. There has been even greater diversity in the suggestions made as to methods for correcting the difficulties thought to exist in the Acts as they now stand. That, of course, was to be expected. Any piece of legislation affects different people in different ways. That is especially true if it is regulatory legislation of the type exemplified in these two Acts. Generally speaking, the suggestions received have been designed to relieve those specific strictures of the Acts that most directly affect the particular group submitting the suggestion. Many of the comments derive from the specific chafing of the restraints imposed. That is only natural. Nobody likes to be regulated even though he may think regulation in general is a good thing.

But the thing that has most impressed us in reviewing the criticisms and the suggestions for change that have come to us in this program of statutory review, has been the extent to which the ideas proposed have been directed not towards eliminating the regulation proposed to be accomplished by these Acts but rather towards making it more practical, more effective and more precisely selective in its application to those whose operations require regulation.

Now obviously all of the suggestions are not in agreement. Indeed there is essential and basic conflict between some of the methods they propose for accomplishing the objectives of the Act. Obviously too we cannot agree with all of them. Most especially we cannot agree with those which, in reaching for practicality, would wholly cripple or eliminate all effective means of restraining practices which it is the purpose of the Act, as far as possible, to eliminate.

But we have gained tremendously in our specific understanding of the detailed problems of people in the securities business by the correspondence and the discussions we have had in connection with this legislative program. I think it is true, too, that many of those from your business who have taken part in these discussions have come to understand more clearly than they did before, not only the objectives of the Acts but the attitude of the Commission and its staff in administering them. I think that they have come also to understand more clearly, and with wider perspective, the problems of their own business as broad national problems, outside the narrow confines of their individual day to day operations. That enhanced mutual understanding, it seems to me, is a very healthy thing. It leads away from the narrow exchange of carping criticism that has characterized the industry's relations with the Commission at times in the past. It can, if it continues, lead towards constructive statesmanship in the field of securities regulation. And, it is likely to lead to the development of increasingly practical methods for accomplishing results which everyone now seems to agree need to be accomplished.

We on the Commission have appreciated the collaboration we have had in our work on these problems far more, I am sure, than those who have given that collaboration have realized. The fact that we don't always agree with what is proposed does not indicate that we reject the cooperation implicit in the offer of suggestions even though we may feel we cannot accept them. We have not completed our study of these problems. Nor have we reached final conclusions

about specific methods for improvement of the present legislation. The interchange of conflicting suggestions highlights the points of controversy. It identifies the difficulties of particular problems and techniques. Frequently it points the way to practical solutions. We have not expected full agreement within the industry. Even less have we expected general acquiescence in suggestions that have occurred to us. We are glad that there has been a free exchange of ideas and free debate of opposite views. That process exemplifies a practical application of the democratic way of getting at problems of this sort. It is a somewhat cumbersome method. It is much more cumbersome and slow than the arbitrary issuance of regulations without consultation, in whatever form they initially occur to a relatively small group empowered to issue them. I think it is likely to produce far better results. But it is essential to the effectiveness of such a system that you who deal with these problems daily in specific situations bring to us freely the benefit of your experience. That kind of experience we can get only from the industry.

I think we have made much progress in this line in the past few months. I think there is an improved sense of understanding between the industry and the Commission. On your part an improved understanding of what we are driving at and how we are trying to get the results that Congress has directed us to achieve. On our part an improved understanding of the practical problems you meet from day to day and a widened perception of ways by which the objectives of the statutes we administer can possibly be achieved while interfering less than they do now with legitimate operations. I think in that respect this has been a good year for the relations between the Commission and the securities industry. I hope that the spirit in which the work done this year has been accomplished will continue and that effective cooperation will increase as we gain in experience and common understanding by working together.

There is one point it would be improvident to forget in enthusiasm for this general subject of collaboration between the Commission and the securities industry. It is impossible for the Commission, if it is to carry out the duties Congress has reposed in it, to overlook the objectives of the legislation it administers. It is impossible for us to neglect, in the interests of practicality, a reasonable probability that a particular proposal will not contribute towards achievement of those objectives, and may nullify them.

There are certain types of activities we are directed to prevent, and to punish if they occur. There are certain types of activities we are directed to require in order that the people buying and selling securities shall have accurate information on which to base their judgment in buying and selling. It is our responsibility to see to it that activities that violate the statutes or frustrate their objectives are curtailed as far as it is feasible for us to curtail them. It is our responsibility to see to it that people dealing in securities are provided with adequate, accurate information essential to the making of the judgments they have to make if their buying and selling are to make sense from the point of view of their requirements. It is almost inevitable that general rules, likely to be effective to accomplish these results, will restrain, to some degree, activities whose motive is not fraud or concealment or overreaching, where the mechanisms employed leave the way open to fraud and concealment and overreaching by those who would use them for those purposes.

We are as anxious as you are to have the restraints imposed interfere as little as possible with legitimate operations. We are as anxious as you are, and probably more, that the applicable rules shall require a minimum of expense and effort for effective enforcement. But in almost all discussions of details or methods we receive suggestions, couched in terms of practicality, whose effect would be to forego, for all practical purposes, the effective achievement of the regulation it is our responsibility to enforce.

I hope you will appreciate the fact that the Commission cannot accede to proposals that would nullify the statute. I think there is a natural disposition on the part of most people -- not all, but most -- to feel a certain distaste for constantly regulating other people's business. There is a not unnatural wish to make concessions to practicality. It is not always easy to insist upon requirements which, although apparently necessary to curtail malfeasance, put burdens and restraints on those who have no thought or impulse to malfeasance. If from time to time you feel, and I am sure you often do, that we are going too far in our regulations, let us know. We are anxious not to go further than we need to go. Perhaps you can show us a better way to do the particular job that bothers you. But consider too whether the regulation you criticize, by forestalling abuses likely to reflect upon the standing and integrity of the business in which you are engaged, may not be likely in the long run to bring you more benefits than it takes away. If you are convinced that it does not then tell us how you think we could do it better. We'd always be glad to know.

Another point I should like to mention before I close deals not so much with the relations between the securities industry and the Commission as with relations within the industry itself. You are engaged in a fast moving, intensely competitive business. It is a business that has numerous and highly diversified subdivisions of function. The process of issuing securities differs materially from trading them after they are issued. Trading on exchanges differs in essential mechanics from trading over the counter. There are numerous divisions of interest within the industry. To some extent there may be a mutual incompatibility of interest between the groups engaged in these different types of operations. To the extent that these differences stem from genuine differences in function and make for genuine competition they are probably a healthy thing. But it's easy for such differences to magnify themselves into

antagonisms beyond the bounds of realistic need. It has occurred to me at times that there is much room in your business for a greater interchange of views among your own divisions, similar to that which has commenced between your industry generally and the Commission. I suggest that you might well consider whether in reality your interests are so far apart from those whose functions in the industry differ from yours, or whose method of operating takes a different form. I have sensed some divisions of thought among you that seem to hamper wholly objective consideration of proposals under discussion with us -- antagonisms that cause aberrations in perspective wholly unrelated to the merits of the proposals under discussion.

A typical example of this sort of thing is the initial approach taken by some of the people in your business to the proposal the Commission submitted to Congress last year recommending legislation extending certain provisions of the 1934 Act affecting reports, proxy regulations, and insider trading to companies not listed on exchanges and having more than 300 security holders and assets of over \$3,000,000.

We have heard few if any objections to that proposal from the securities industry which attack, on the merits, the idea that investors in such securities should have available the kinds of information those provisions would require the issuers to make available to them. Instead the industry objections to these proposals have been almost exclusively the outgrowth of concern for competitive relationships within the securities business -- primarily the fear that the extension of these requirements to securities of large enterprise to which they do not now apply would drain from the over the counter market, into exchange trading, securities now available exclusively for off board trading.

There has been some objection, too, on the part of houses that specialize predominately in a limited number of securities about which they have

special access to special information. There have been other questions raised about this proposal, equally based in concern lest the result of the proposal would be to take away some present special advantage over competitors in the industry. Whatever may be said for these objections as they apply to the special interest of those who raise them, they are plainly not based on any concern for the welfare of the ultimate owner of the securities.

Recently there have been some indications from the industry, that perhaps the opposition to these proposals might be diminished if there were to be considered along with them some modification of existing practices affecting the determination of what securities shall be traded on exchanges and what securities shall be traded exclusively over the counter.

I don't propose now to discuss the merits of the main proposals. From the point of view of investors they seem to me to be meritorious beyond serious question. Nor do I propose to discuss the merits of the collateral controversy which these proposals raise.

I do suggest that the two questions are quite separate questions and should be considered as such. And I wonder whether the securities business itself does not have sufficient statemanship to focus its attention on the only problem these proposals seem to raise as far as your business is concerned -- the problem of division of the market for the securities that would be affected -- and work out some suitable suggestion for dealing with that question.

I point to the possibility of candid consultation within the industry on this question merely as an example of the sort of thing that would benefit from the development of a closer community of viewpoint within the securities business itself, and from a common appreciation of the fact that fundamentally you are all engaged in carrying out, in various ways, parts of a function in our economy that is essential to its continued well being.

You know as well as I that many operations in carrying out that function are not now performed as efficiently or as fairly as they might be. You know that many things go on that are inimical to the interests of the public investors from whose patronage, ultimately, you make your living. I wonder whether it wouldn't be better that you be alert to work out, within the industry, ways to eliminate those things which, in the long run, can do your business nothing but harm, rather than to wait for the spur of government regulation. Internecine feuds over division of the spoils can accomplish little in the long run except to bring the entire industry under criticism and perhaps subject it to regulation more drastic than would be needed if the forces of self-restraint within the industry were as effective as they might be.