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SECURITIES AND EXCHANGE COMMISSION
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THE SECURITIES TRANSACTION PROCESSING ACT OF 1972

An Address by

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I am grateful for this opportunity to be able to speak before you today. This is particularly so because the Securities and Exchange Commission has found that a critical part of the securities industry, the paperwork side, in which banks are significant participants, requires closer attention. I would like to discuss with you the proposed legislation which the Securities and Exchange Commission recommended to Congress on March 22nd of this year concerning the processing of securities transactions. It is referred to as the "Securities Transaction Processing Act of 1972" and it has been introduced in the Senate by Senator Williams joined by Senators Bennett and Tower. I am sure it will be of interest to you as it involves regulation of the transfer agent industry and those entities performing securities depository and clearing functions. It also addresses itself to the manner in which broker-dealers process securities transactions and would confer upon the Commission authority over the form and format of the stock certificate.

As we are all aware banks handle a significant portion of the transfer agent work. While securities depositories and clearing agencies are now exclusively operated by

exchanges, banks and trust companies are potential participants in these functions as well. In fact, there are plans to spin-off the largest securities depository (CCS), an affiliate of the New York Stock Exchange, into a New York Trust Company, to be owned jointly by banking and securities organizations. The major New York clearing house banks and several other banks located outside of New York City are already participating in the collateralized loan program of the New York depository. It is becoming increasingly apparent that it is important for banks to participate in this collateralized program in order to handle the loan business of New York Stock Exchange broker-dealers. These same forces may compel banks to eventually expand their participation in depositories with regard to other securities transactions.

These developments obviously have significance to you as bank regulators. Will the investment public and the participants in these vehicles of progress be adequately protected as they expand their functions over settlement and banking activities? Will they be operated efficiently and fairly? Who is to have the responsibility for regulating these entities as they evolve? What will be the responsibility of State bank regulators?

I would like now to give you some background regarding the legislation which the Commission has proposed to Congress. Prior to 1967 little attention was given to the processing of securities transactions. It was a low priority item for broker-dealers and for banks as well. The profits were to be achieved elsewhere, and the best management talent was not deployed in securities processing or, as it was commonly called, the "back office" of these businesses. Predictable consequences followed. During the 1967-1970 period, there occurred the most prolonged and severe crisis in the securities industry in forty years. During this critical period more than a dozen NYSE firms failed and customer losses exceeded $130 million. In the face of these losses public confidence dwindled rapidly. It became imperative that something be done to restore public confidence, and it was in this context that the Securities Investor Protection Act of 1970 developed. This Act protects customer funds and securities left with broker-dealers up to $50,000 for each customer, and Congress placed $1 billion behind the SIPC Corporation to accomplish this objective.

With a potential exposure of $1 billion of public funds and the possibility of still another crisis, Congress quite properly instructed the Commission to undertake a study of the causes of these losses and financial instability and report back its findings and suggestions for corrective legislative action. The Study of Unsafe and Unsound Practices of Brokers and Dealers was submitted to Congress by the Commission in December of last year. This Study revealed that the then existing system for processing securities transactions was inadequate to handle the rising trading volume. Delivery, clearing and transfer facilities became hopelessly clogged as they proved unequal to the increased volume, and failures of all kinds accummulated. It is in this context that the Commission recommended to Congress the legislation dealing with the entities which process securities transactions.

There is an urgent need for a unified securities processing system to prevent the recurrence of the back office crisis. The legislation we have proposed has as its first objective the prevention of further loss to

investors through a break down of the securities processing system and protection of the $1 billion of public funds committed to the SIPC program. But our objectives extend beyond these. We expect to see positive benefits flow to all participants from the rapid development of privately owned systems. Here we are talking about greater efficiencies and lower costs. The Commission is concerned with the rapidly rising costs of doing business in the securities industry and its adverse effects upon profits and services. Let's take a look at some fundamentals. For five years, from 1962 through 1967, brokerage costs per transaction increased a little less than $5 from $27+ to $32. Then in 1968, the transaction cost jumped $6, in 1969 another $5 and in 1970, $7. After holding transaction costs to less than a 20% increase over five years, transaction costs jumped over 50% in three years. Clerical and administrative costs per transaction went up 5% over the five years, 1962-67 and 40% over the next three years. I am sure your constituents, the banks, have experienced similar cost problems.

The electronic facilities developed by the banking industry for processing and clearing checks and for safekeeping and transfer of government securities exemplify what has been done to fight rising bank costs and how modern technology can be used in the economic processes. Both activities have required close integration with the operations of commercial banks, and each has involved relatively long periods of gestation. We can learn much from your experiences as we seek to apply similar concepts to the securities processing area. We are mindful, however, of the complexity of our task. United States Government securities and cash involve only one issuer -- the U.S. Government, whereas in our efforts to oversee the development of an integrated securities processing system we must deal with tens of thousands of issuers and the numerous and unique legal problems, tax questions and operational complications tied into this fact.

Just as banks and the public have experienced benefits from the systems for handling checks and Government securities, we would like to see similar advantages arise from our efforts. The collateralized loan program of

CCS which we referred to earlier is a beginning. If we as regulators can work with the private sectors to accomplish the goal of a nationwide securities processing system, significant cost reduction should follow for banks and for members of the securities industry.

Enormous saving may also occur as we immobilize or eliminate the stock certificate. The Commission's authority over the form and format of the stock certificate is an important element of the bill. We are told that the BASIC program of building a system of regional depositories, with banks and brokers throughout the country participating, can reduce stock certificate movement 75%. Responsible and knowledgeable people inform us that conversion from a certificate to an electronic record and a printout can cut back office costs by 70%. But, in my view, even these savings are overshadowed by the compelling need to be ready to handle the 50 million share days we will have if we are to satisfy the capital needs of the second half of this decade. In short, ladies and gentlemen, we want to see these positive benefits inure to the banks, brokers, and other participants in the securities process, and ultimately to the investing public.

As you can see, the Commission's recommended legislation is predicated upon the continuation of privately owned and operated entities performing clearance, settlement and transfer functions. We have made this choice because a significant portion of the banks and other entities comprising the securities industry have already demonstrated that they are embracing modern communications and computer technology to the extent achievable under present conditions. The Commission feels that the basic ingredients for a modernized securities processing system already exist.

What is needed now is a force to direct and accelerate the evolution of these private efforts into a single, integrated and nationwide system of securities clearance, settlement and delivery. It is our view that the development of depositories and clearance systems now operating and being planned, and the functions of transfer agents and other entities involved in the securities handling process must be controlled and directed in a manner which keeps each system open-ended and compatible with other systems in order that they may perform at maximum levels and service the entire investment community. Regulation

of the process as a whole is clearly desirable, and the Commission, having traditionally exercised statutory responsibility over the broker-dealer community, investment companies, stock exchanges, securities associations, issuer companies and those entities now performing clearance, settlement and depository tasks, is in the best position to oversee the development of a unified securities processing system.

It should be emphasized that the Commission does not contemplate new regulatory burdens upon depositories, clearing agencies and transfer agents. Rather, as the provisions of the bill indicate, the opposite is true. The requested authority to establish minimum standards fall into four categories: first, performance of functions, second, with regard to non-bank entities, measures and personnel standards for safe handling and custody of securities and funds, third, operational compatibility with others, and finally, as may be appropriate, non-discriminatory access. In most cases, the minimum standards which we hope to see established will be readily met by those already in the business. In setting minimum standards we will give careful consideration to the then existing capacities and economic impact. As

a first step we might call for a standardized form of the stock certificate if it could be demonstrated that economic savings would inure to transfer agents and others. Obviously, immobilization of the stock certificate is an even higher objective, and assuming it could be done without infringing upon the safety of the investors' holdings, we might call for the elimination of the stock certificate in the settlement process.

We have done several other things in preparing this legislation to minimize regulatory impact. First, and most important, we do not seek to interpose government in the securities process itself. We believe that private efforts will accomplish the ultimate goals sought. The Commission would not wish to be in a position of having to build a government organization to take over these functions. Second, the requirements of registration called for in this bill, while applying indiscriminately to both bank and non-bank entities, are designed to be met without great effort. In this regard, banks, which act as transfer agents, will register with the Federal Reserve, the Federal Deposit Insurance Corporation or the Comptroller of the Currency, depending on the bank's

status. Reporting requirements and inspections of banks performing these functions will be the responsibility of bank regulators.

The bill contemplates a vital role by you as State bank regulators. It specifically states that nothing in it shall impair the authority of State banking authorities with regard to their exercise of regulatory or supervisory oversight over banks performing depository, clearing agency or transfer agent functions. The bill further requires that the Commission and the Federal bank agencies having responsibility for compliance with the bill's provisions must take into consideration any program of inspection, examination and enforcement carried out by State banking authorities designed to insure compliance by banks with its provisions. We will be asking you to assist us in making this legislation work. Your guidance and expertise as to the fiscal responsibility and the safe handling of customers' funds and securities by entities performing transfer agent and depository work are particularly important to us.

To the extent State bank regulators now have or plan to undertake an inspection and reporting program regarding bank depositories or transfer agents designed to meet the objectives of this legislation, the Commission would hope to be able to work with you to avoid duplicate regulatory oversight and undue burden upon banks. The Commission does not wish to expand its jurisdiction to conflict with or supplement that of Federal or State bank regulatory agencies. We believe the bill reflects this wish. Our objectives have been clearly stated: to see that a national system for the settlement of transactions is implemented as rapidly as possible and that the final system is non-discriminatory, as efficient as practicable, and serves the needs of the investment community. We solicit your support for the bill and your continuing assistance thereafter.

Thank you.