

CAUTION - ADVANCE

FOR RELEASE UPON DELIVERY

ADDRESS

of

ROBERT E. HEALY

Commissioner, Securities and Exchange Commission

before the

OHIO VALLEY GROUP

of the

INVESTMENT BANKERS ASSOCIATION OF AMERICA

at

THE LOUISVILLE COUNTRY CLUB
LOUISVILLE, KENTUCKY

8:00 P.M., C.S.T. -- May 2, 1939

41844

The past two decades have seen a substantial growth in that portion of our population which is interested in securities. During this period an increasing number of new security issues found their way into public hands. The ownership of private or closely held businesses was more and more shared with others through new stock issues. Whereas prior to this period the investment and securities business had depended on a relatively few wealthy customers, estates and trust companies, in the past twenty years more and more of the general public became stock and bond buyers. With this expansion in the numbers of investors, the business of supplying them with securities and providing them with a market place has grown apace. This growth, as we all know, brought with it many new problems.

In line with this growth was the increase in the number of brokers and dealers engaged in the securities business, an increase in the number of securities and an expansion in the physical plant and equipment of the securities business. To a great extent, particularly outside of the exchanges, this growth was disorganized, sporadic and at one time progressed beyond the needs indicated by public demand. If there was extravagance it was indulged in by exchange members as well as by over-the-counter brokers and dealers and it evidenced itself in the multiplication of sumptuous offices, in the employment of large numbers of salesmen and in large outlays for extensive advertising. Naturally the overhead expenses of brokers increased and when the securities business fell off in line with other business, this enlarged plant made adjustment to the changed times difficult. Although at first the public may have footed the bill through inordinate profits taken by dealers, the unhealthy situation eventually affected the business and served further to retard the volume of trading and to discourage investment.

In this connection one might well raise the question as to whether or not the trend of public habits in security buying and investment has not begun to show signs of a reversal to the conditions which prevailed twenty years ago. This is undoubtedly a question to which all of you have already given serious thought. One cannot overlook such indicators as the great growth in recent years of insurance company holdings and savings bank investments. I mention this merely in passing because I feel that we should not accept too readily the belief that the average investor will, of his own accord, remain an active security buyer.

All of us recognize that the average investor has in recent years seen a great many things which would have the effect of destroying his confidence. I refer to many abuses which ultimately led to the passage of the Securities Act of 1933 and the Securities Exchange Act of 1934 and to the establishment of the Securities and Exchange Commission.

Basically the purpose of the law and of the Commission, as I see it, is to maintain such standards of honesty and decency in the securities business as will merit the confidence of investors and the public. This purpose the Commission has been pursuing, at the same time having a proper regard for the smooth functioning of the securities markets, for the prosperity of the business and for the soundness of its position in the national economy.

The securities business flourishes when the nation's industries expand. The business problem which confronts you as security dealers is the problem which confronts every major industry - how to increase production and volume profitably. I do not pretend to be able to give you the solution to this business problem, but I do feel strongly that against the background which I have just described, one great forward step which the over-the-counter business could take at this time would be the formation of a strong, well-knit association such as that contemplated by the Maloney Amendment to the Securities Exchange Act.

As you know, the idea of a national association, voluntarily founded and self-administered to carry out the aims of the Securities Exchange Act grew out of discussions between our Commission and leaders of your profession. With this in mind Senator Francis T. Maloney of Connecticut proposed and Congress approved an amendment to the Act to permit the formation of such an organization under the law. What we of the Commission hope will be achieved is that the standards of business applicable to the over-the-counter markets will be raised and that these higher standards will be made uniform throughout the nation. We could have asked Congress for powers to improve such standards from above, but it seemed preferable that you be given the opportunity to adopt them by self-government under a statute which would not contain the constitutional defects which wrecked the National Recovery Act in the courts. The Commission has, since the passage of the Maloney Act, actively encouraged the formation of voluntary associations. We believe that brokers and dealers can provide improved services to the public by the mechanism of such voluntary organizations; we feel that improved business should compensate the costs thereof. In fact, it seems to us at the Commission that your investment in such an organization would bring you fair returns. One of the points which we have been discussing relating to the organization, is the question of costs. It is evident that as usual you must pay for what you get. If you are to have an effective organization, you must consider its cost as you consider the costs of your own business and economize only so far as you do not impair the efficiency of the outfit.

Another point of discussion relates to the personnel of the organization itself. We feel that to be effective, it should be manned by persons who are efficient, impartial and who are willing to make their work with the organization a quasi-public career. Just as you as security dealers devote all of your time to your own business, so, we feel, those in charge of an association ought to give all of their time to the business of the association.

I have heard it said that it is the desire of the Commission to see at the head of a securities association someone who, to use the popular phrase, would be a "Charlie McCarthy" for us. That is not true. The Commission is strongly opposed to the notion that the executive officer of a national securities association should be the dummy or the nominee of any group. Rather he should represent the national interest of the securities business in its best and broadest form. He should not be a "Charlie McCarthy" for anybody; and neither should he be the sort of honorary figurehead that some groups suggest, a meaningless titular head who serves no one well and leaves the organization the prey of conflicting interests within the industry.

The Commission further feels that the standards set for the over-the-counter business should be uniform throughout the country and that the small dealer should on a small scale provide service and protection to the public equivalent to those provided on a large scale by the larger dealer; that, conversely, the larger unit should have no privileges nor advantages which are not shared by the small. We have been told that some of the opposition to the

formation of voluntary associations emanates from fear on the part of the small dealers that the large underwriting houses will dominate the organization. This fear should be dispelled for I doubt that the Commission would grant registration to an association whose organization made such a result possible.

There are those among you, I think, who believe that the government should regulate the over-the-counter business directly. Recently, representatives of the national securities exchanges have been urging this step upon us. With some justification, they maintain that the over-the-counter business should be subject to the same standards of business conduct as stock exchanges and that they should be governed by the same public safeguards as those imposed upon exchange members. They have cited examples where exchange members have lost business to over-the-counter dealers because the rules were applicable to the one and not to the other. Direct government regulation, they say, would place all upon an equal footing. The Commission, as you know, has thus far adhered to the belief that the same end could be accomplished through a system of self-discipline under government supervision. The Commission, however, has powers to supplement the enforcement program of the voluntary associations so that there may be uniformity under the law. The amount of direct government regulation which may be necessary will, of course, depend upon the character and accomplishments of the association or associations which are organized.

Another desirable standard for a voluntary association is that its membership be representative of all classes of the business. Should the members of an association be predominantly of one class or group, it will fail of its purpose. Indeed it would be unfair that the trade preferences which attach to membership in an association should be restricted to just a few dealers.

The security dealers of the country, it seems to me, face a unique opportunity to effectively organize their business. The need for such organization is widely recognized. The regulations which have been imposed by stock exchanges and by the Commission upon exchange members have been popularly applauded. Although the character of the over-the-counter business is not precisely similar to that carried on by stock exchange firms, it is clear that, from a national standpoint, the problem is of equal importance.

The organization of an association is a task primarily for the industry itself. If such an organization is established and if under the law it is registerable the Commission will register it. On the other hand the Commission is under a duty to carry out the mandate of the statute and it will be unable to register any association which does not promise the standards of business practice called for by the statute.

The Securities and Exchange Commission has a public duty under the law. You, as security dealers, have a responsibility to the public which you serve that its funds and securities shall be protected throughout the industry by the same high standards of dealing which now guide its best elements. If the over-the-counter business cannot get together and work out an effective organization, the Commission faces its clear duty to work directly to the end that over-the-counter markets shall afford the same degree of protection to the public which is provided by regulation of stock exchanges. The choice is clearly yours. We shall continue to work with those who are striving to build an effective organization. We shall try to solve the difficulties of those who are opposed. We hope that before long we shall see our joint efforts bear fruit. We hope the results will be of benefit both to you and the public you serve, that cooperation between your business and my Commission will be a practical operating reality and that it will make a valuable contribution to industry and the public welfare.