Address of

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I don't need to tell members of the securities industry that their business deals in something deeply affected with a public interest. The business always has been affected by a public interest and it keeps getting more so.

For one thing, more and more people have direct or indirect interest in investments. Look at the growth of investments by union welfare and pension funds and life insurance companies, not to mention the mutual funds. For example, it is estimated that 90 million individuals hold life insurance policies and 53 million hold savings accounts. Also, 14.5 million hold some form of annuities or pension plans -- all of which are, to a considerable extent, invested in corporate securities. These indirect holdings are in addition, of course, to almost 8 million individuals who own stocks.

The interest of direct and indirect investors, however, is only a part of the great public interest in the field of raising and administering capital. The securities markets provide the medium for the formation of capital from the savings of the people.

One characteristic of the American economy which has helped produce the standard of living which our people enjoy (and I apologize for over-simplifying) is constantly improving methods of production based on research and replacement of obsolescent equipment. This makes for mass production for a mass market so that the luxuries of one generation become necessities for the next. To keep our capital plant growing and improving, to maintain the expanding economy we now enjoy, there must be a continuous flow of new investment capital into our economy. While retained earnings and cash throw-offs are the major source of funds to build and replace plant and equipment, continuing new infusions of capital are necessary for the economic blood stream.

Basically, continued investment requires continued public confidence in the processes of capital formation.

The investor from your standpoint must be a satisfied customer. That is more than a platitude. He must have such well founded confidence in you and in our system of distributing and trading in securities that he will understand losses without bitterness and resentment just as he appreciates profits. You know and I know a few people who today with some bitterness decline to buy securities because of what happened almost 25 years ago. That bitterness -- fortunately now encountered only rarely -- is rooted in lack of confidence.

The success of your efforts and the efforts of state and Federal securities administrators, when appraised in terms of contribution to the economy, must be measured by the confidence which those efforts inspire in the American investor and by the extent to which that confidence is deserved.

Appreciation of the position and importance of the investor is expressed in a statement made last September by a strong and responsible leader of American labor, David J. McDonald, President of the United Steel Workers of America, who said:

> "We are engaged in the operation of an economy which is sort of a mutual trusteeship . . . The United States Steel Corporation has almost as many stockholders as it has employees. These stockholders employ a group of managers . . . Certainly the managers must give full consideration to the just claims of the workers. Certainly the working force must see to it that the steel properties are operated successfully because if they are not . . . they will have no jobs. Both . . . have an obligation to the stockholders . ."

The mutuality of interest between those who earn money by work and those who invest money is evidenced by the spread of employee stock ownership and, in some cases, the introduction of stock purchase plans as a subject for collective bargaining. Reduced to simple terms, a great many of the

people who work for their living are the self-same people who are investors.

All of this amounts, of course, to a series of truisms, but the truisms are those about which we should constantly keep reminding ourselves. This widely diffused direct and indirect public participation in the capital markets, plus the obvious necessity of maintaining public confidence in our processes of capital formation and capital management, make it clear that the laws governing the securities markets must be administered vigilantly in the general public interest and not for any one or more special groups, however articulate the groups may be.

The Commission over which I have the honor to preside, is vested with a number of powers to make rules and regulations necessary or appropriate in the public interest and in the interest of investors. When we consider those rules or when we consider public comments received on proposed rules or when we have public hearings or conferences about rules or policies, we must always bear in mind that we represent all of the segments of the public which are not represented by the groups which are urging a particular course of action upon us. I say these things not as an adverse comment upon the many fine suggestions which have come to us from the several organizations of the securities business, but merely to indicate the compelling necessity for our Commission to be objective.

But let me leave a discussion of our Commission's philosophy for a moment in order to turn to your part in this process of creating in the American investor a merited confidence in our system of capital formation and management.

I have made a number of speeches here and there, about the basic philosophy of disclosure which runs through the Acts administered by our Commission. I don't need to tell you how disclosure is required in registration statements, offering circulars, annual reports, interim reports, proxy statements. All of this is based on the doctrine that people should be given the facts and left to make their own

decision. I submit that that is a sound philosophy but it works well in practice only if

1. The facts get through to the people, in this case the investors, and

2. They understand the facts.

The accomplishment of both these objectives in the sale of securities requires both sound administrative and selling practices and a long educational process.

The securities laws have worked well both during the period of economic convalescence and the present period of energetic health. But like everything else, they could work a lot better.

The good results which the securities laws produced are due in part to the fact that those who have much to do with determining the price which investors are willing to pay for securities, do read and understand the information which is furnished. In other words, the material in registration statements and financial reports is examined and understood by investment bankers, by analysts, by investment advisers, by institutional investors, by the conscientious dealers and by many sophisticated investors. However, the comment made by William Z. Ripley in 1926 in his book "Main Street and Wall Street" is still too true:

> "The advocacy of really informative publicity as a corrective for certain of our present corporate ills must be placed in its proper relation to the whole matter of democratization of control. A prime argument which raises its head at the outset of all discussion of shareholders' participation in direction is that the shareholder -- the owners, in other words -- is hopelessly indifferent to the whole business. His inertia as respects the exercise of voting power, and almost everything else, is an acknowledged fact. But no one expects it to be otherwise. No one believes that a great enterprise can be operated by town meeting. It never has been done successfully; nor will it ever be. The ordinary run of

> folk are too busy, even were they competent enough. Nor is it true that the primary purpose of publicity, the sharing of full information with owners, is to enable these shareholders to obtrude themselves obsequiously upon their own managements. But such information, if rendered, will at all events serve as fair warning in case of impending danger. And this danger will be revealed, not because each shareholder, male or female, old or young, will bother to remove the wrapping from the annual report in the post, but because specialists, analysts, bankers and others will promptly disseminate the information, translating it into terms intelligible to all.
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> " . . . This, then, is the ultimate defense of publicity. It is not as an adjunct to democratization through exercise of voting power, but as a contribution to the making of a true market price. This is a point but half appreciated at its real worth."

Mr. Ripley's statement, while written in the framework of a discussion of shareholder voting, was, and unfortunately is, applicable to the investor's failure to dig out and understand the facts which are available to him when he makes his investment. I entertain, and you entertain, few delusions that human nature can suddenly change. People still sign neighborhood petitions without reading them. Too many fail to read their insurance policies. And so I suppose the same human trait causes people to neglect the opportunity to find out the facts about companies in which they invest their money.

As a result the American investor does not get enough of the primary benefit of learning the facts about the companies in which he puts his money. He depends too much upon the secondary benefits, that is, the contribution to a fair market price made by the fact that people of special aptitude, dealers, analysts, and the like, have read and do understand the information which is furnished.

If we are to depend upon disclosure for the protection of the investor, you and we both have responsibilities to help the investor get the maximum benefit from disclosure.

People cannot be forced to read prospectuses before they buy. But something ought to be done to give them a prospectus to read if they choose. A businessman acquaintance of mine, a man who is a typical intelligent middle-class investor, just last week told me that he couldn't see much use of all the work which the SEC did to assure adequate prospectuses, if the investor got the prospectus only after he had bought the security. I am sure that none of us would argue with the logic of the complaint. In fact, that problem, over the years, has provoked more discussion than any other administrative problem confronting the Commission. As I will point out later, the 1954 amendments are designed to contribute to its solution.

The whole waiting period theory of the Securities Act was to provide a time after the registration statement has been filed and before it becomes effective during which a prospective investor may become familiar with pertinent facts relating to the issuer and the underwriting.

It was in furtherance of this objective of disseminating information about the issuer and the underwriter during the waiting period that the "red-herring" prospectus mechanism, and more recently, the short-form identifying statement were devised. The 1954 amendment to the Securities Act, embodying principles on which there has been general agreement between the Commission and the industry since 1941, was intended to give a firmer statutory basis for pre-effective dissemination of information and to give the Commission greater flexibility in permitting summaries and condensations of the pertinent material set forth in full in the registration statement.

The amendment in no way affects the legal provisions which have existed up to now by which the full statutory prospectus must be furnished at the time the sale (as distinguished from the mere offer) is consummated.

I would like to stress, with as great emphasis as I can put on it, the fact that the 1954 amendment does not permit the pre-effective use of sales literature which has not been filed with the Commission and processed by the staff. We have been disturbed since the amendment became law because in several instances issuers and underwriters have sent out unprocessed sales literature prior to effectiveness.

The amended law was not intended to permit pre-effective "free writing". This was a subject briefed by industry representatives and thoroughly discussed with the Commission when we were serving as advisor and consultant to the Senate Banking and Currency Committee and the House Interstate and Foreign Commerce Committee in connection with formulation of the bill. The proposal of industry representatives that the Securities Act of 1933 be amended to permit pre-effective "free writing" was rejected.

The testimony presented by me on behalf of the Commission and by various representatives of industry groups reflects clear understanding on the part of the Commission and the industry that pre-effective "free writing" was not intended to be permitted in the future any more than it has been in the past.

Speaking generally, the aim of the amendments to the Securities Act is to give a more definite statutory recognition to the practices which had been prescribed over the years by the Commission for pre-effective dissemination of information. The statute provides rule making power in the Commission to permit short-form summary prospectuses or preliminary prospectuses which, we hope, may be susceptible of more rapid processing than the so-called "red herrings". The definitive rules on the subject are currently in the process of formulation, and I am not prepared at this time to draw on my gift of prophecy to indicate the precise form they will take. However, administrative processing of summaries and preliminary material seems inherent in the concept of the amended statute.

Since that is so, the timing of the use of such material by the underwriters must be influenced by the practical fact that administrative processing consumes time. The flow of

business into our Division of Corporation Finance is something we cannot control, and our staff is limited. Pressures build up at particular seasons such as the proxy season. But our intention, both as to formulation of rules and as to processing techniques, is to accomplish so far as possible the purpose of the amendment to foster broader dissemination during the waiting period of information about forthcoming issues.

But in another way you and we are faced with a challenge -- you in your selling techniques and we in our administration of the Act -- to see that securities are sold on the basis of the most completely informative data practicable. By encouraging the use of preliminary processed prospectuses, the 1954 amendments, with the cooperation of the industry, can result in the investor receiving a higher grade of information than the "bare-bones" material of the identifying statement or the oral statements of the salesmen. If that end can be accomplished we aid in the spreading of greater financial literacy among American investors.

Up to this point, in discussing disclosure and furnishing of information to investors, my emphasis has been on disclosure in the selling of securities. As you know, however, under the Securities Exchange Act of 1934, the Commission is empowered to require annual and interim reports from listed companies and companies which have registered securities under the Securities Act of 1933. At the present time an annual report is required and current reports are required in respect of certain corporate changes.

The Commission this week is circulating for public comment a proposal which, if adopted, would require semi-annual statements of operating results and surplus from companies which are listed on national securities exchanges or which have registered securities under the Securities Act of 1933. Under the proposal, one additional financial report per year would be required from such companies. This would be a semi-annual condensed profit and loss and surplus report. You may recall that in 1952 the Commission proposed a rule calling for quarterly statements of profit and loss and earned surplus instead of the quarterly statement of gross sales or revenues on Form 9-K. There was considerable opposition to the proposal because of the inherent difficulty in supplying

accurate, detailed figures on an interim basis and because of the civil liability which might be imposed in respect of estimates which proved erroneous. Consequently, the proposal was not adopted. In the fall of 1953, the Commission discontinued the requirement for quarterly statements of gross sales or revenues because, among other things, of the fact that gross figures may run counter to net results and the gross figures may, therefore, be misleading. From a number of quarters there have come requests -- from investment bankers, dealers, analysts and statistical services -- that the Commission reinstate the quarterly reports of gross operating results or interim reports of net operating results. The proposal as circulated attempts to meet many of the objections made by registered companies to the 1952 proposal for quarterly statements of net operating results. The new proposal provides for condensed data and provides that such reports, since they are necessarily based in part on estimates, shall not be deemed "filed" for the purposes of Section 18, the section which imposes civil liability in respect of such reports.

Comments on the proposal are solicited before February 28 and a public hearing will be held on March 9. We hope to hear from both proponents and opponents of the proposal.

General knowledge of the operation of the capital markets on the part of growing numbers of our people plays a part in maintaining the health of our economic system. It is analogous to the part played by wide-spread technical competence in the fields of production, engineering, and construction. People who understand something about the securities they buy and the companies which issue them and who understand how securities are sold and how they should be sold contribute to a public opinion which advocates sensible rather than extreme regulation.

I present all of this in the hope that something in these remarks may provide a stimulus to your fundamental thinking. You and we are playing a part in such an important activity of American life that we should keep asking ourselves time and again why we do what we do and what we can do better.

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