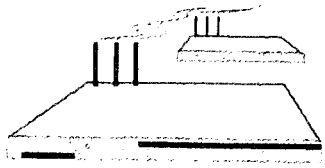

NEW STEPS TO STRENGTHEN THE RIGHTS OF STOCKHOLDERS..

By
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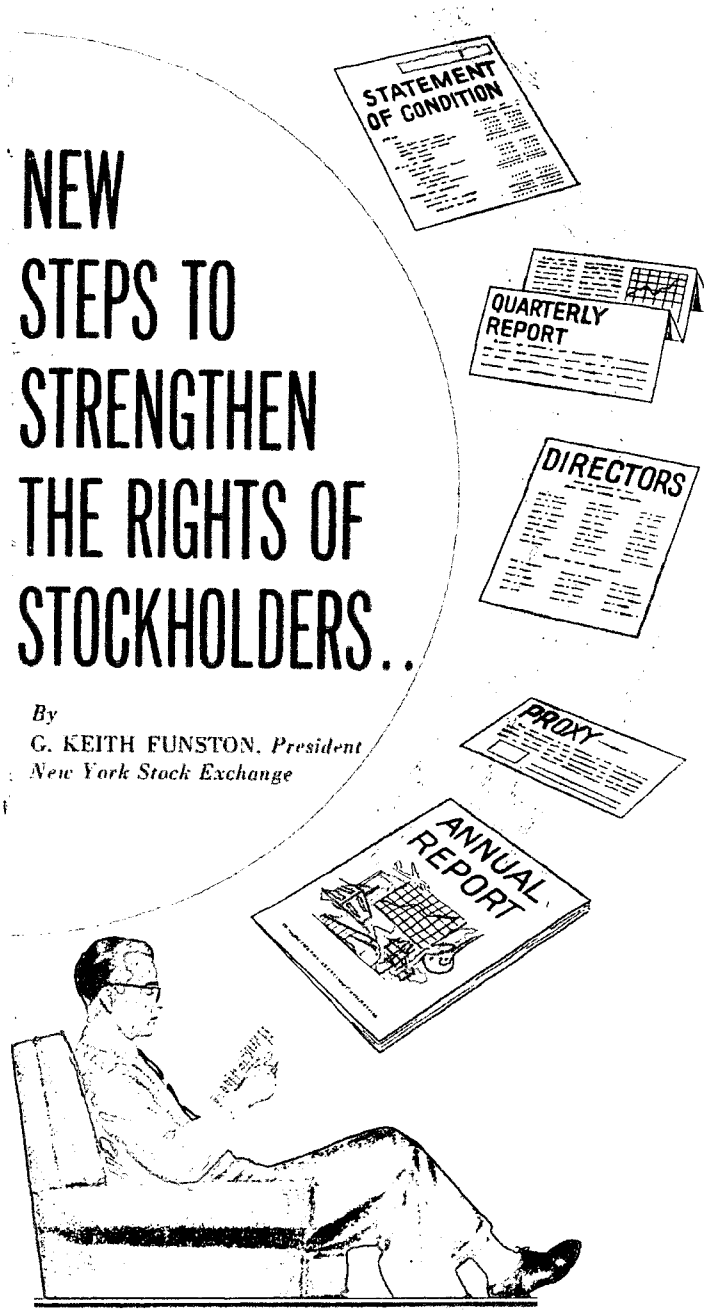
New York Stock Exchange



Remarks by G. Keith Funston

President, New York Stock Exchange

before

General Management Conference, American Management Association

Hotel Statler, New York City

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THERE is a woman in Dallas, Texas and a man in Galloway, Ohio—two people I have never met—who really suggested the text for most of my remarks today.

Not long ago I received brief notes from each of them. The Texas letter proclaimed that the Stock Exchange's effort to broaden the ownership of business was helping create a new dimension for America's economy and for its people. The Ohio letter was somewhat more personal. The writer had purchased shares in a small appliance company several years ago. He noted that he had neither heard from the company nor had he been able to obtain any information about it. He wondered how he could remedy this.

In these two letters, it seems to me, we can trace some of the enormous *progress* we have made—and some of the real *problems* we have fallen heir to—as corporate ownership has expanded. My Texas correspondent reflects the attitude of millions of people who are coming to a new understanding of our remarkable economic system. But today it is the man from Galloway who concerns me most. For he symbolizes the problems some investors still face, even despite our great progress. Those problems, briefly, concern the rights of stockholders . . . the matter of full disclosure . . . and the question of proxies and proxy contests.

In any given month we are apt to receive, at the Stock Exchange, several letters that have a disturbing sameness to them. They

———QUOTATIONS FROM THE TEXT———

I have asked myself often—why, indeed, can't all stockholders vote? Why isn't more financial data available to the owners of all securities, and not just to those listed on a national exchange? . . . I am convinced that our form of democratic capitalism is undergoing one of its more dramatic tests. That test, very simply, is whether the rights, privileges and duties of a nation of shareowners can be developed properly and safeguarded.

Our point of view is clear and consistent. We believe that if the mass of our people are to risk their dollars on the nation's growth, there is no moral justification for depriving any shareowner in any publicly-held business of a corporate vote.

It is not enough merely to extend the vote. It must be extended in a way that makes it easy for the shareowner to cast his ballot on a wider range of issues—without traveling half-way across the continent to vote in person at an annual meeting.

We believe that in proxy contests the SEC should be given the legal teeth to make sure all participants meet its disclosure requirements. Specifically, we believe the SEC should be empowered to go to court and seek a temporary restraining order barring the vote of any stock in which the Commission has reason to believe any proxy participant has an undisclosed interest, either direct or indirect . . . We can also bar practices which amount to the purchase or sale of proxies.

Let me acknowledge that the suggestion to restrict the corporate vote, even under the circumstances I have outlined, is not made easily. But there is no question, either, that investors have the right to know who contest participants are, how much stock they control, and how they acquired it.

The proposed Fulbright measure is a means of developing a set of disclosure standards which—while not as comprehensive as those of the New York Stock Exchange—will give all shareowners more of the data they have a right to receive.

New safeguards will also mean new responsibilities for shareowners. They will have to cope with more information, make hard decisions, cast their votes and know what they are voting for.

pose questions that go something like this: "Why wasn't I allowed to vote?" "Why didn't I receive a proxy?" "Why can't I get more information about my company?"

It is small comfort to reply that these safeguards have been largely provided for investors only when the securities they own are listed on the New York Stock Exchange. For the basic questions remain. After all, of the many thousands of publicly-held companies, only eleven hundred are listed on our Exchange. And I have asked myself often—why, indeed, can't all stockholders vote? Why isn't more financial data available to the owners of all securities, and not just to those listed on a national exchange?

These issues are as timely as this morning's newspapers. And they form the basis of several proposals I am anxious to explore with you—proposals which, if adopted, can strengthen immeasurably our system of free enterprise.

That system, I might add, has attained its great strength because we have managed to keep it free. It has made its greatest strides as we have struggled to make it more democratic. Indeed at the present time, I am convinced that our form of democratic capitalism is undergoing one of its more dramatic tests. That test, very simply, is whether the rights, privileges and duties of a nation of shareowners can be developed properly and safeguarded.

Corporate Enterprises Must Respond to the Will of Millions of Investors

Let's look for a moment at just two of the economic changes since World War II that bring this problem into focus.

First, it is apparent that not the few, but the millions, enjoy an astonishingly high standard of living. The nation's families, with greater funds at their disposal than ever before, are not only living better *today*, but they are saving, investing and planning for *tomorrow*.

This has led to a *second* vital development. Shareownership has mushroomed. Through institutionalized savings, about 110 million Americans now are indirect owners of business. More important, over 8.6 million people are direct shareowners in our publicly-held businesses. This represents a sharp 33% increase over 1952. And the single most important fact we have learned about the nation's shareowners stresses both the appeal and the spread of ownership: two-thirds of our stockholder family have incomes under $7,500 a year.

At the Stock Exchange we believe with some justifiable pride that our concerted and careful education program in recent years has done much to encourage such shareownership on a sound basis. But we are well aware that in the coming decade corporations will need extraordinary amounts of growth money to meet their future needs.

Our appraisal of the decade ending in 1965 is that some $60 billion in outside equity money should be raised for new plants and equipment alone. This sum is triple the new stock financing in the last ten years. It is beyond the capacity of our financial institutions to furnish it. Thus, it is clear that industry must reach out to the mass of the American people. It must encourage the investment habit. As this is done, we will develop, much more than at present, a "People's Capitalism." As the profits of the future are distributed more widely, a newer, better and more productive order of things will inevitably emerge.

But there is an important "if" to the promise of our future. As our corporate form of enterprise develops further, it must do so along democratic lines. It must be responsive to the will of additional millions of investors. And to be responsive, I submit that these basic conditions must be met:

First, shareowners must be *assured of a corporate vote*. The reason was put very

simply by an English writer recently. He said: "intelligent investment is not conducted best by mutes."

Second, shareowners must be given the machinery and the convenient opportunity to exercise that vote. This means insisting that proxies be provided to shareowners of all publicly-owned businesses.

Third, management should be urged to submit for shareowner approval, the vital proposals affecting a corporation's future.

Fourth, because proxy contests for corporate control are a necessary part of the democratic process, the ground rules for *fair and honest proxy contests* must be further developed and spelled out.

Fifth, shareowners must be assured of *adequate and timely information* on which to base their vote—and in a larger sense—on which to base their investment decisions.

Finally, investors must be assured that the basic safeguards established for their protection *will apply to all publicly-owned companies,* regardless of whether their shares are traded on a national stock exchange or in the over the counter markets.

It is these points I should like to concentrate on.

All Shareowners Entitled to Vote, to Receive and Cast Proxies Conveniently

At the outset let me make clear that the Stock Exchange is not—and has not been—naïve about the difficulties or even the dangers of an expanding shareownership along democratic lines. The democratic process is never easy or automatic. But within the area of our own responsibility the Stock Exchange has made considerable progress. Indeed, the philosophy we have helped develop is a measure of how far 20th Century capitalism has progressed.

When it comes to the *ballot,* for example, the New York Stock Exchange has refused, since 1926, to list common shares not carrying the right to vote. Today, every common stock listed on our Exchange carries voting rights. Within the past few weeks our Board of Governors decided on two further steps. *First,* we will refuse to list the common voting shares of a company which also has non-voting common stock outstanding in the public's hands. *Second,* we will consider delisting the common stock of a company which creates non-voting shares. Our point of view here is clear and consistent. We believe that if the mass of our people are to risk their dollars on the nation's growth, there is no moral justification for depriving *any* shareowner in *any* publicly-held business of a corporate vote.

And it is not enough merely to extend the vote. It must be extended in a way that makes it easy for the shareowner to cast his ballot on a wider range of issues—without traveling half-way across the continent to vote in person at an annual meeting.

At the Stock Exchange we have, over the years, successfully taken two courses of action in this regard that make our position unmistakably clear. *First,* we have succeeded in broadening the number of vital corporate matters that must be submitted to shareowners for their approval. As a result, our listed companies now seek stockholder approval before issuing new securities in connection with executive compensation plans. They also must obtain stockholder approval before issuing substantial blocks of stock to acquire another company. And finally, a stockholder vote is necessary before issuing any stock to acquire another business in which officers, directors or large stockholders have an interest.

The *second* thing we have done is to persuade virtually all of our listed companies to *solicit proxies.* In 1955 we made compulsory proxy solicitation a part of our *new* listing agreements. At present, of the almost 1100 corporations on our Board, only 43

active companies do not seek proxies. In a good many cases these companies point out that from 50 to over 90% of their shares are in concentrated holdings. Hence, they believe that proxy solicitation would serve no real purpose. The Exchange does not agree. We think minority stockholders are especially entitled to express their vote and to do it conveniently by proxy. Accordingly, we shall continue to employ moral suasion to convince the balance of our listed companies that the public interest demands proxy solicitations.

PROPOSE SEC BE GIVEN POWER TO ENFORCE DISCLOSURE RULES IN PROXY CONTESTS

If we agree that shareowners are entitled to vote simply and easily, I believe we must also take a realistic look at the question of *proxy contests.* There are several specific proposals in this area I should like to make. But I want to preface them with two observations. The *first* is that our recommendations are weighed neither in favor of management nor in favor of those opposing management. Rather, our concern is that the individual shareowner receives the data he needs to express adequately a measured opinion. His freedom of choice is our most important consideration.

My *second* comment is that although the problems of proxy contests are very real indeed, they ought not to be magnified out of proportion. For example, among the New York Stock Exchange's approximately 1100 listed companies there were only 6 contests in 1954, 9 in 1955 and 8 in 1956. Thus, while the changes we want to urge are in many ways sweeping, they are essentially designed to head off a relatively small number of future abuses.

In this connection, however, my own position is very much like that of the elderly gentleman who surprised his friends by suddenly taking off on a tiger-hunt. "You can't realize the excitement," he said later, "of walking through a thick jungle and never knowing when a tiger is going to leap out."

"How many tigers did you shoot?" he was asked.

"None," he said.

"Then the safari was a failure."

"Listen," came the reply. "When you're hunting tigers, *none* is plenty!" In like terms, no abuses are plenty when we're developing our particular form of corporate democracy.

Today, the rules of the Securities and Exchange Commission hold that when proxies are solicited by listed companies they must contain full information. In proxy contests for the election of directors, these rules require detailed information concerning the identity of participants in the contest, their stock holdings, and their commitments and agreements concerning the stock or the company. These are important pieces of information for each shareowner to have. Where domestic stockholdings are concerned, the Commission can enforce these rules and insure disclosure by use of its power of subpoena and the penalties of perjury. But these enforcement powers end at our geographic boundaries. And we have seen a strange situation develop recently. Where shares are held in the name of foreign institutions, either for U.S. citizens or nationals of other countries, the SEC finds itself frustrated. It cannot get the facts, force their disclosure, or pierce the anonymity of accounts held by foreign institutions.

To overcome this barrier we believe that in proxy contests the SEC should be given the legal teeth to make sure all participants meet its disclosure requirements. Specifically, *we believe the SEC should be empowered to go to court and seek a temporary restraining order barring the vote of any stock in which the Commission has reason to believe any proxy participant has an undisclosed interest, either direct or indirect.*

There are several merits to this suggestion. The first is that the difficulty of piercing

the anonymity of foreign holdings—at least during proxy contests—would be eased measurably without directly involving the foreign institutions. It should be remembered, moreover, that foreign institutions are themselves often prohibited by law from revealing data the shareowning public should be aware of.

Another advantage to this suggestion is that it would place the burden of deciding whether to make full disclosure or sacrifice the vote directly where it belongs on the true beneficial owner.

Finally, the proposal would not invade unnecessarily the privacy of investors who are not participants in the contest. There are those who prefer for convenience, safekeeping, or other personal reasons to have their shares registered in the names of banks or brokers. Their desires must be respected.

Let me acknowledge that the suggestion to restrict the corporate vote, even under the circumstances I have outlined, is not made easily. But there is no question, either, that investors have the right to know who contest *participants* are, *how much stock* they control, and how they acquired it.

There is another area in which we need equally forceful action. It concerns a practice which is unthinkable in the political area—and against which there are no adequate safeguards in corporate elections: the sale of votes or proxies. Under present conditions such abuses are clearly possible.

Well, the buying or selling of proxies should be prohibited by law. And I believe this can be accomplished if the Congress were to pass legislation prohibiting the voting of any stock which, in effect, is involved in the purchase or sale of a proxy, and which was not financed in accordance with the Federal Reserve Board's margin requirements. To enforce this law, the SEC would have the power to go to court to seek an injunction blocking the vote of the stock in question.

If the court found that such a purchase or sale had been made, the vote of that stock would be prohibited. In short order the ability to buy or sell the corporate vote would become remote.

Passage of Fulbright Bill Would Spur Flow, Timely Data to More Owners

A final question concerns us greatly. It involves the kind of timely data available to shareowners, and the ease with which it can be obtained.

The Exchange itself is no Johnny-come-lately to this problem. We do, in fact, take a kind of perverse pleasure in a letter in our archives dated 1866. In it, in answer to a general request the Exchange had made for copies of reports issued to stockholders, a corporate official had replied with simple dignity: "This company makes no reports and furnishes no statements." Period!

I hardly need stress the extent to which our listed companies—and many others as well—have made timely disclosure a basic ingredient in our economic system. Since 1900 the Exchange has required all listed companies to furnish annual reports. For over 50 years we have urged issuance of quarterly reports as well. Over 90% of our companies comply. The exceptions, by and large, are engaged in seasonal businesses. In addition, since 1932 the Exchange has insisted that annual financial statements be prepared according to sound accounting procedures.

Over the years the cumulative effect of these measures has resulted in an informed and articulate group of shareowners. We believe that *all* shareowners are entitled to these safeguards. But they are guaranteed generally *only* to owners of securities registered on a national Exchange. For the millions owning shares in thousands of unlisted companies, however, there are no such assurances. Whether or not they receive regular financial reports and details about proxy

contests . . . whether or not their vote is solicited or even allowed at all, are questions left to the discretion of individual companies.

If statistics are needed to dramatize the lack of data available about unlisted companies, consider the SEC's 1956 report on the practices of unlisted companies. Of 663 large unlisted corporations whose proxy solicitation material was studied, it was discovered that *73% did not even identify nominees for directors running for election. Moreover, in 52% of the cases where major proposals were to be voted on, the proxy form did not provide for a negative vote. Stockholders had the option of voting for the proposal, altering the proxy, not voting at all, or attending the meeting in person if they wanted to cast a negative ballot.*

The obvious conclusion to be drawn is that one standard exists for listed companies and a second standard for companies that are not listed. And inherent in this double standard are potential abuses that can only serve to disenchant the investing public.

Last March the Exchange moved to do something about this double standard—at least to the extent of our authority. Our Board ruled that when members of the Exchange community participate in proxy contests involving *unlisted* companies they must furnish information similar to that now required by the SEC of listed companies. In addition, our Board decided our members may not be associated with a non-member in an unlisted company proxy contest, unless the non-member agrees to supply the same material required of our members. By these actions we believe important strides can be made towards providing shareowners of *unlisted* companies with the data they are entitled to—*at least where our membership is involved.*

Only in Washington, however, can the issue be met head-on. And Senator Fulbright has come to grips with it in a proposed bill

now being considered by the Senate Banking and Currency Committee. Under terms of this measure, unlisted companies with more than 750 shareowners and over $2 million in assets would have to file periodic financial reports. They would have to comply with the SEC's proxy rules. They would have to report stock transactions by company officers, directors and large stockholders. The Fulbright measure, in short, is a means of developing a set of disclosure standards which—while not as comprehensive as those of the New York Stock Exchange—will give all shareowners more of the data they have a right to receive.

Proposed Steps Will Dramatize Development of a "People's Capitalism"

In the proposals I have outlined there is one thing, of course, we must recognize. It is that strengthening the rules that govern our corporate affairs won't automatically produce a cure-all for our problems. The burden of making a democratic system work must rest, as it always has, on the people most intimately involved—in this case on the nation's shareowners. It is an old story but true, that "bad officials are elected by good citizens who do not vote . . ." Thus, building new safeguards will also mean new responsibilities for shareowners. They will have to cope with more information—much of it complicated. They will have to make hard decisions, cast their votes and know what they are voting for. None of these things, however, appears to be a matter that should deter us.

For, by and large, year in and year out, the average American has demonstrated he is a mighty resourceful and thoughtful person. Give him the facts, and the opportunity and the machinery to exercise his judgment and we don't have to worry about the end result.

In summary, this is what I have been anxious to stress:

Using the yardstick of ownership, our great publicly-held companies have already gone democratic. They are owned today by over 8.6 million people. They must be owned tomorrow by additional millions able and willing to supply our extraordinary need for growth money. One of the great challenges we face is to keep our corporate machinery responsive to the will of these millions of owners. In a number of areas we have the opportunity today to demonstrate that we mean business when we say we are determined to strengthen the rights of shareowners.

We can take steps to obtain the right to vote for every owner of common stock.

We can insist that he is entitled to vote conveniently on important issues—through proxy solicitation.

We can help insure—during proxy contests—that participants make complete disclosure by giving the SEC the authority to ask a court to block votes unless the Commission is satisfied its rules are being met. We can also bar practices which amount to the purchase or sale of proxies.

We can see to it, apart from proxy contests, that investors get the full and prompt information necessary to sound decisions.

And finally, we can provide that these necessary safeguards apply to all publicly-held companies and not just to those which happen to be listed on a national securities exchange.

By taking these steps we can do a great deal to underscore for our own people and for the world what we mean by the words, economic democracy or People's Capitalism. We can prove to my correspondent in Galloway, Ohio, that our corporate affairs are, in fact, influenced by the small, everyday acts of millions of unpretentious men and women. And we can show him that we are indeed concerned with his needs and with his rights as a stockholder.