THE KEY MAN IN BROADENING SHAREOWNERSHIP

Remarks by G. Keith Funston, President, New York Stock Exchange, at the 20th Annual Convention of the National Association of Investment Companies, Savoy Hilton Hotel, New York City, Thursday evening, October 13, 1960.

Twenty years ago when you gentlemen of the NAIC took, so to speak, your first toddling steps as an organization, I doubt that anyone would have dared predict the giant strides you would make in a single decade. Ten years later when you had already demonstrated your capacity for prodigious growth, I wonder who would have foreseen the continuing giant strides ahead? And now, with investment companies managing a gigantic total of $17 billion in assets and with a record number of 2,500,000 individual shareowners, I am still moved to ask: who can be bold enough to project the future which will be yours by 1970?

For what has happened over the last two decades opens new dimensions for the years ahead. The years gone by have not been years of economic growth only. They have been years of psychological growth as well. Somewhere in the early 1950's, Americans turned an important emotional corner in their attitudes about investing. After a long period of skepticism, the average family no longer asks the hesitant question: "Why <u>should</u> we own stocks?" Today the question is: "Why shouldn't we?"

I stress this change of attitudes for a very cogent reason. When we look ahead to the prospects for shareownership in 1970, it is not primarily the barrier of "economics" which sets our limits. The purely <u>economic</u> possibilities are enormous. Rather, the factor most likely to determine the extent of shareownership is one of attitude, of inclination, of motivation, of confidence.

As you know, in the 1959 Census of Shareowners, the Stock Exchange estimated that about 12.5 million individuals owned stocks in publicly-held companies. Perhaps less familiar to you are the attitudes expressed by non-shareowners in a still more recent survey. They reveal that for every existing stockholder, there is today another individual who is on the threshold of investing. In addition, there is a second group of nearly 23 million people whom we must consider. Although not quite to the point of making an investment decision, this group is definitely interested in such investment techniques as Employee Stock Plans, Investment Clubs, MIP and other stock purchase programs.

This is a body of potential shareowners which stretches the imagination. But note that today they are only potential investors. Our problem, therefore, is to gear up the securities industry to serve responsibly the needs of this huge audience. Our task is to help catalyze the public's general goodwill into the hard stuff of individual decisions. The question as to whether they should or should not invest must be resolved in a manner which will be rewarding to the individual and to our nation's economy.

What will that catalyzing agent be? Part of it - and a part which intimately concerns you - will be the skill with which investment managers handle the billions of savings that have already been entrusted to you. Yet skillful investment management alone will not be enough. Equally important will be the direct personal experiences of millions of new investors in dealing with a registered representative, a securities salesman or other investment advisor. And it is these experiences which will be crucial in determining whether the shareowning potential of the 1960's becomes a mutually productive reality - or a bungled opportunity.

The Challenge to the Securities Industry

I do not think that opportunity will be bungled. The growth in shareownership over the past decade would not have taken place if many millions of new investors had not formed satisfying relationships with the sales representatives of the securities industry. Yet I would be remiss if I did not point out that the scene is changing. Customer relationships in the future will be more rigorously tested than in the past. And as one economist has written, "The modern free enterpriser must constantly adapt not only his product but also his business philosophy to a changing reality If this adaptation is to be successful, it must be visible not only in the memos of top management, but at the public periphery as well. It is here that the enterprise meets and wins its customers." This is an admonition which bears particular relevance to our industry. As I have already pointed out, the dimensions of our market have changed. Our industry must adapt to these changes.

The number of people in the securities business handling public accounts has risen from an estimated 30,000 in 1950 to slightly over 100,000 this year. Part of that increase has occurred among registered representatives of New York Stock Exchange member firms. Part lies within the growing ranks of members of the National Association of Securities Dealers Perhaps the largest percentage increase consists of the sales people who have been added to the staffs of mutual fund distributing companies.

This increase in total personnel is in itself both a necessary and a healthy development. A rising demand for a service naturally brings in its train a larger service organization. But in the case of our particular industry, I think we will agree that a growing demand requires more than just a larger quantity of people. It also requires a greater emphasis on the quality and training of our people.

For we must recognize that most of tomorrow's shareowners - now hesitating on the verge of ownership - have never before talked with a member of the securities industry. Many of them still entertain old fears and misconceptions about securities as a personal asset. Some of them believe in securities - but for the wrong reasons. Others, despite good levels of education, are uninformed about - and ill at ease with - what they consider the mystifying language of investing.

To these millions of potential owners, the first contact with an industry representative will be crucial - not only in terms of their own investing habits, but in terms of our own prospects for future growth. A customer who feels high-pressured, over-sold, under-informed will not stop to consider whether the investment he was persuaded to make might not have been a sound one. He will feel that he has been "had" - and he is likely to take out his resentment, not just on a particular individual or firm, but on the securities industry as a whole.

Thus, the challenge to our industry is not to motivate ten or twenty million one-shot customers out of the vast potential market. It is to create ten or twenty million additional long-term investors. Nor is the selling of securities the challenge we face. The challenge is to emphasize the opportunity to own securities - and to understand the risks and rewards involved - as a proper and prudent means of self-advancement.

Have We Met the Challenge?

How well has our industry met this challenge? Let's start by looking at the spectrum of registered representatives and securities salesmen today.

About 32,000 people handling client accounts are employed by member firms of the New York Stock Exchange. They are full-time representatives, subject to the stringent responsibilities assumed by these member firms. They handle a wide range of securities, from conservative bonds to highly speculative stocks. Their function is not to be a "salesman" in the orthodox sense of the word. Rather, it is to help their customers in selling securities - as well as in buying. Before registered representatives can handle any securities business for the firm's customers, they must be screened, not only by their employers, but also by the Exchange itself. Before being fully accredited they must complete a training program ordinarily taking about six months. They must pass a written examination given by the

Exchange.

Apart from the Stock Exchange community, 55,000 producing personnel work for organizations which are members of the National Association of Securities Dealers. They include, incidentally, the majority of the selling personnel of mutual investment companies. These sales people must evidence certain minimum qualifications by passing a written examination given by the NASD.

In other words, of the industry's entire national selling force, only some 15,000 are not subject to a minimum qualification established by the industry itself. But that does not mean that all in this group are inadequately prepared. On the contrary, many work for firms which provide good training of their own. But some of this group have apparently received little or no training. These are employees of firms which have chosen not to join hands with an exchange or the NASD and which are not required by law to do so because they do not deal with other brokers or operate entirely within the confines of a single state.

In addition to the industry requirements, there is a certain safeguard in the various state registration systems. Although limited and uneven, this structure also helps establish and maintain standards.

This, in the large, is the picture of the people in the industry who today are handling the public's business. I will touch on some of the weaknesses in a moment. But first it is important to call attention to the basic strength in this structure - the fact that the great majority of our industry has voluntarily accepted the responsibility for setting up and testing the qualifications of its own sales people. All in all, the picture is an encouraging one. As a national stereotype, the old-time "customer's man" deserves to be filed away in the nation's scrapbook.

But this is not yet a complete picture. Despite this testing, there still exists a certain number of people who operate in a vacuum of responsibility. The securities they handle may be excellent. The techniques by which they handle them sometimes are not.

What are the questionable practices I refer to? Let me mention a few examples:

From Connecticut: A foreman at a local industrial plant was putting pressure on assembly line workers to buy funds from him.

From Florida: A woman was told by a door-to-door novelties salesman that a stock he handles was distributing capital gains the next day and rushed her into buying shares for this purpose.

From New Jersey: A postman who also sells a mutual fund tried to persuade a 63-year-old mechanic to invest his entire $5,000 savings in a 10-year, front-end load contractual plan.

I think I need not go on. There is the problem. The number of such cases may not be large, but I need hardly remind you of the damage which even a few well-publicized instances can cause And now the question is: What can we do about it?

<u>What Is To Be Done?</u>

Let me begin by making clear that this is a problem which goes far beyond the specific excesses I have mentioned. It is not just that the practices of one small part of our business must be improved. The challenge, rather, is how best to elevate further the level of responsibility throughout the entire industry. We are, after all, not only united in the public eye, but knit together by the relationships of our business life. Member firms of the Stock Exchange, for example, handle about 30 per cent of all mutual funds. The mutual funds, in turn, constitute one of our most important customers. Hence we must recognize that the <u>quality</u> of the personnel in any one part of the industry affects us all - raising us all up together, or subjecting us all to a common criticism. This holds true whether we are conducting back office operations, managing investment portfolios, or participating directly in dealing with the public.

Because this problem affects us all, I think you may be interested in what the Stock Exchange has recently begun to do. It is a three-part program:

The first calls for further raising our minimum qualifications for registered representatives. To this end, early this year we asked a leading testing organization to analyze our present examination and to tell us how it could be strengthened. On the basis of pilot tests which are now well under way, I expect that new, tougher examinations will be ready by January 1, 1961. In addition, they will be administered through a nation-wide network of testing centers.

The second phase of our program calls for providing newcomers with the up-to-date tools they will need to master the more demanding qualifications we are going to insist on. By way of preparation, we are helping our member firms broaden their individual training efforts. In addition, we are working with leading universities in New York, Chicago, Los Angeles, Boston, and other major cities in developing new courses for registered representatives. These classes, by the way, are open to qualified people throughout the industry.

Third, we are concentrating major efforts on the continuing personal growth of those registered representatives already experienced in the business. Through conference programs and refresher courses for partners and registered representatives, through the preparation of new materials, and through a clearing house for sharing training techniques developed by individual firms, we are seeking to reach every corner of our community.

These steps will, I believe, lead to a more genuinely professional level of training for Stock Exchange registered representatives. That is what we believe is required in order to serve the new investing public in the years ahead.

But what of other segments of the industry? Our common interest prompts me, at least, to ask a few pointed questions.

First, the National Association of Securities Dealers last year raised the passing grade on its examination from 70 to 80. The NASD is now considering making its basic test more difficult. These are vital and welcome steps. But should not the NAIC take advantage of this period of reassessment to urge particularly that the test be broadened to include a more comprehensive coverage of mutual funds? Should not this test call on mutual fund salesmen to demonstrate a searching knowledge of their field?

Second, what about the overall problem of supervision? I do not doubt that most firms today offer excellent training and supervision of their account personnel and that they intend further improvement. This applies both to firms which belong to NASD and those which do not. But what of the few indifferent or careless firms? What of the harm that may be caused by their untrained, over-zealous sales personnel? Would it not protect the interests of every member of the NAIC to prevent this sort of mis-representation? And could this not best be accomplished if the NAIC itself undertook the responsibility for defining a set of standards that spell out the qualifications and controls for people handling mutual fund shares? I daresay that such a step would not only greatly enhance the public esteem of your organization, but would also attract additional investment companies who wished to share in that esteem.

If the past is any guide, I think we can safely say that the surest way to avoid onerous regulation is for the industry itself to make every effort to keep out of the business those who may seriously damage its reputation.

One development we might well look towards, I believe, is the establishment of a national securities examination. This would have a core of questions covering principal areas of knowledge essential for everyone in the industry who handles public accounts. Each and every applicant would take this portion of the examination. A separate section could embrace

Stock Exchange questions only and would be taken only by those seeking approval by the Exchange as registered representatives. Another section could be developed by the NASD dealing with the over-the-counter market and mutual funds. Any duplication of questions could be eliminated and each applicant would take those necessary parts of the examination for which he sought registration. And, finally, the examination itself could be given at common testing centers.

This exam could serve the responsible self-regulating sections of the securities industry. And it could be available to states as well - for use with those personnel who are not covered by the industry's own testing mechanism.

The Stock Exchange will, in fact, have available early next year just such a test based on its studies to date. It will cover the essential features of what eventually could be included in a national securities examination given by the industry. Indeed, if this forthcoming exam will be of assistance to those states which even now are studying their own testing procedures, we will be pleased to make it available.

There is one final point I should like to cover. As a "growth" industry, the securities business has attracted to its fringes some people who are manifestly unable to provide sound investment guidance. Furthermore, their ability to reach the necessary level of competence is limited by the fact that they have only a part-time commitment to our field. The major demands on their time are in other, often unrelated, fields.

At the Stock Exchange we believe that it is not possible to exercise adequate controls unless our member firms employ registered representatives on a full-time basis. Put another way, we don't believe that the public can be adequately advised about selecting securities by someone who devotes only a small share of his business day to the complex problems of securities investment.

Can someone earning his basic living as a clerk-typist, diaper salesman or window trimmer qualify for the exacting job of providing sound investment advice? Even though of first-rate ability, has he the necessary time to achieve that qualification and keep up to date? I think these questions are not too difficult to answer.

It seems to me the very least the securities industry must demand for itself, if it employs part-time help to handle customers' accounts at all, is to select its part-time force from among first-rate people in those occupations which are already concerned with some phase of broad, over-all financial planning such as accounting or law.

What Is At Stake?

I may seem to have come a long way from my opening remarks about shareowning prospects for the middle 1960's. Yet I would like to stress again that those prospects will not materialize automatically from haphazard doorbell ringing or telephone calling. Indeed, unless tomorrow's investors are guided by well-trained, intelligent as well as forceful people, I think we will not realize our potential, or attract the permanent, long-range investors we want.

This need not happen if we act affirmatively. But it will require that all of us attend to the problem at hand.

If I may summarize the situation:

First, the size of our industry's immediate potential market is at least equal in numbers to the present shareowning population. But to turn this potential into an actuality will require not just more selling, but more responsible selling and servicing. It must aim at not just more shareowners, but better-informed shareowners. The key man for achieving such goals is the registered representative or sales person who goes out to meet the public.

Second, the Exchange is stepping up its efforts to meet this problem in its own area in a number of ways: by seeking to toughen its examinations for registered representatives...by encouraging more comprehensive member firm training programs...and by developing greater educational opportunities for new as well as experienced personnel.

Third, the framework exists for similar efforts elsewhere in the industry - by upgrading and broadening NASD's examination...by further improving individual training programs...by developing a stringent code of standards for NAIC members...and ultimately by preparing a national securities exam covering the basic knowledge essential for the securities salesman - an exam which could be given at testing centers set up at key points across the country.

Finally, in its own self-interest, the securities industry should aim towards insisting eventually that people handling client accounts are full-time employees. In the interim the industry should employ, to deal with the public, only those whose principal business is concerned with some phase of broad over-all financial planning.

One final word. No program designed to improve the quality of service can confine itself merely to technical training. The most productive man in an organization is not always the man who sells the most securities. He is the man who helps the right people select the right amount of the right securities for the right reasons. At the heart of the matter is a moral commitment - a commitment to the idea of sound and broader shareownership, a commitment which goes far beyond matters of immediate economic gain.

What I have outlined is perhaps a far-reaching program. But these are not times when lesser solutions recommend themselves. I would like to see our industry, propelled by its own private initiative and guided by its own enlightened conscience, reach higher and harder than ever before.

We have met our responsibilities well in the recent past. Top management in our industry continues to show its eagerness to meet them in the future. But, in the words of the economist I cited earlier, it is not enough for management to write memos. The test is to transfer that eagerness to the public periphery where an enterprise meets and wins its customers. Here is where the challenge of the future lies.

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