THE EFFECTS OF ORGANIZATIONAL RESPONSE ON DEPROFESSIONALIZATION: THE CASE OF STOCKBROKERS 1975-1990

by

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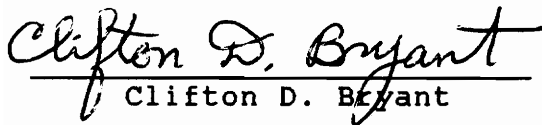

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(ABSTRACT)

This study investigates organizational response as a mediating factor in the relationship between environmental change and deprofessionalization of stockbrokers between the years 1975 and 1990. Both quantitative and qualitative content analysis are used to analyze 412 business news articles concerning three brokerage firms.

It is hypothesized that the environmental changes of jurisdictional competition resulting from deregulation of the industry, technological changes, and declining client trust resulting from scandals, will not have a direct effect on deprofessionalization of stockbrokers in these firms. It is expected, instead, that these environmental changes will be mediated by organizational responses, resulting in

variation among the firms in the deprofessionalization of stockbrokers. The quantitative portion of the study shows different patterns of organizational response among the three firms examined regarding the environmental changes being investigated. The qualitative portion of the study indicates variation in deprofessionalization for stockbrokers within these firms resulting from differences in organizational response.

The results of this study suggest a need for further investigation of the effects of organizational responses on the extent of deprofessionalization for professionals working in organizations. Organizational responses are likely to influence not only stockbrokers but other professionals in times of change and flux due to events both internal and external to the organization.

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TABLE OF CONTENTS

	Page
Abstract	ii
Acknowledgements	iv
Table of Contents	vi
List of Tables	x
Chapter 1 Introduction	1
Statement of Problem	6
Significance of Problem	8
Research Questions	10
Chapter 2 Review of Literature	11
Professionalization	11
Trait Perspective	12
Process Perspective	15
Power Perspective	17
Deprofessionalization	21
Systems Perspective	24
Strategic Choice Theory	28
Environmental Factors Influencing Deprofessionalization	30
Jurisdictional Competition	31
Jurisdictional Competition and Deprofessionalization of Stockbrokers	34
Changes in Technology	37

	Changes in Technology and Deprofessionalization of Stockbrokers	39
	Declining Trust	42
	Declining Trust and Deprofessionalization of Stockbrokers	45
	Organizational Employment of Professionals	46
	Statement of Hypothesis	51
Chapter 3	Methodology	52
	Comparative Approach	55
	Firms Chosen for Comparison	57
	Merrill Lynch & Company	57
	Drexel Burnham & Company	57
	Charles Schwab & Company	59
	Data Collection	60
	Quantitative Analysis	64
	Qualitative Analysis	67
	Reliability and Validity	69
	Summary	70
Chapter 4	Quantitative Analysis	72
	Jurisdictional Competition Associated with Bank Deregulation	76
	Movement of Bankers into Areas Previously Limited to Stockbrokers	76
	Movement of Brokerage Firms into Jurisdictions of Other Professions	78
	Banking Services	78
	Insurance Products	87

Real Estate 88

Competitive Strategies 90

Low Cost 92

Full Service 94

Special Niche 96

Mergers and Acquisitions 98

Adoption of Changing Technology 102

Information Services 104

Program Trading 109

Market Services 110

Scandals 113

Insider Trading 115

Junk Bond Fraud 117

Other Types of Fraud 118

Multiple Types of Fraud including Insider Trading 120

Other Multiple Types of Fraud 120

Churning 121

Company Indicates Solution 122

Summary 125

Chapter 5 Qualitative Analysis 131

Charles Schwab 133

Control and Content of Work 133

Effects of Scandals on Company Reputation 137

Effects of Organizational Responses on Deprofessionalization 146

Drexel Burnham 141

Control and Content of Work 142

Effects of Organizational Responses on Deprofessionalization 144

Effects of Scandals on Company Reputation 147

Merrill Lynch 149

Control and Content of Work 150

Effects of Scandals on Company Reputation 156

Effects of Organizational Responses on Deprofessionalization 159

Summary 163

Chapter 6 Conclusions 166

Responses to Environmental Changes 169

Bank Deregulation 169

Technology 170

Scandals 171

Effects of Organizational Responses 172

Deprofessionalization 174

Suggestions for Future Research 175

LIST OF TABLES

		Page
Table 4.1	Articles for Years 1975-1990 Frequencies and Percentages by Firm	73
Table 4.2	Stockbroker Movement into New Areas Frequencies and Percentages by Firm	79
Table 4.3	Competitive Strategies Frequencies and Percentages by Firm	91
Table 4.4	Adoption of Technology Frequencies and Percentages by Firm	103
Table 4.5	Types of Scandals Frequencies and Percentages by Firm	114

CHAPTER 1

INTRODUCTION

The occupation of stockbroker has played an important part in the history of the United States, serving as a vital link between buyers and sellers in the financial marketplace. During the period from the establishment of the New York Stock Exchange in 1792 until the stock market crash of 1929, there were increases in size, number, and diversity of publicly traded corporations along with gains in prestige for stockbrokers (Clews 1973; Snowden 1987). The 1929 crash decreased trust in stockbrokers and brought about a call for reform in the financial market system. This reform movement led to federal securities regulation through securities acts passed in 1933 and 1934.

Before the 1929 stock market crash, stockbrokers were respected for their financial expertise (Clews 1973), but there is no indication that they were considered to be professionals. In fact, the first systematic attempts to study professions came early in the 20th century. During the 1920s and 1930s social scientists were just beginning to look beyond the traditional professions of medicine, law and the ministry to analyze other occupations in terms of the process of professionalization (Vollmer and Mills 1966:12).

The following are identified as characteristics of professions as opposed to occupations: highly specialized training in preparation for provision of essential, exclusive and complex services based on a body of theoretical/abstract knowledge, autonomy, authority over clients, ethical codes, and legal recognition (Greenwood 1957; Goode 1957, 1960; Wilensky 1964; Forsyth and Danisiewicz 1985). Although stockbrokers had financial knowledge and offered financial services prior to 1929, in the period following the 1929 stock market crash they began adding other professional characteristics.

In the early 1930's the occupation of stockbroker exhibited a number of characteristics associated with the process of professionalization. The service they provided was considered essential, or of serious importance, to clients. The service was exclusive, with the monopoly being provided by federal securities regulations. The service task was complex rather than routine, since it involved discretionary application of specialized knowledge (Wilensky 1964; Jamous and Peloille 1970; Johnston 1972; Forsyth and Danisiewicz 1985). Although stockbrokers offered many of the same services before and after the 1929 crash, two differences led to increased identification of stockbroker services as professional. First, federal securities regulations were created to establish jurisdictional boundaries for stockbrokers. Second, the stockbrokers

organized themselves in ways to protect the jurisdictional boundaries that were thus put into place, including efforts to demonstrate to the public that the service-task is essential, exclusive, and complex.

This organization is evident in the formation in 1939 of the National Association of Securities Dealers, Inc. (NASD), a registered national securities association. The National Association of Securities Dealers, Inc. provides a code of ethics for stockbrokers, and membership is denied to any broker-dealer who is operating in an improper or unethical manner. One of the primary purposes of the NASD is to administer and enforce "rules to prevent fraudulent and manipulative acts and practices, and in general to promote just and equitable principles of trade" (Loll and Buckley 1981:412). Brokers must be registered with the Securities and Exchange Commission (SEC) to be eligible for membership in the NASD, and operations of the NASD are supervised by the SEC (Loll and Buckley 1981:410). In addition to the NASD, disciplinary proceedings can also be brought by a number of other regulatory groups including the SEC, stock exchanges and state governments (Foust 1993).

A licensing program, which required stockbrokers to be licensed by the New York Stock Exchange and by individual states, provided protection of jurisdictional boundaries by controlling access to the profession. Wilensky notes that professional knowledge is often judged by being able to

prove competence to "an agency external to the hiring firm or consumer" (1964:138). Licensing formalizes monopoly and uses the authority of the state in enforcing exclusive jurisdiction. In fact, compulsory licensing is considered "the most comprehensive form of legal monopoly" (Rothman 1987:76).

As early as 1956 the National Association of Securities Dealers, Inc. set up minimum membership requirements, including the passing of a written examination, the General Securities Exam (Loll and Buckley 1981:ix). Among the topics covered by the examination are various types of investments (stocks, bonds, options, etc.), regulations and procedures, economic and security analysis, and the operation of securities markets. Passing the General Securities Exam is a requirement for licensure by the New York Stock Exchange. In addition to this exam, approximately half the states require an additional licensing examination (Eaton 1987:41). Since the time of their inception, these entrance standards have become progressively more difficult (Loll and Buckley 1981:ix).

In addition to a professional organization with a code of ethics, stockbrokers have been able to maintain a degree of autonomy within the bureaucratic organization of brokerage firms. For the most part stockbrokers are in non-salaried positions outside the management hierarchy of their organizations (Kurland 1991). Generally, brokers are able

to rely on their own judgment concerning financial advice and selection of financial strategies for their clients. Until banking deregulation in the 1970s and 1980s, the regulations of the securities acts of 1933 and 1934 helped to protect stockbrokers' areas of professional knowledge from intrusion by others.

In spite of these characteristics of professionalization, in recent years the process of deprofessionalization has been evident in the profession of stockbroker. The deprofessionalization thesis proposes that professions are losing their position of trust and prestige (Freidson 1984). The concept of deprofessionalization is based on an assumption that professions are clearly different from other occupations. Proponents of deprofessionalization argue that there has been a decline in the distinctiveness of professions, and a progressive loss of special characteristics. Haug points to specific types of loss for professions, including losing "their monopoly over knowledge, public belief in their service ethos, and expectations of work autonomy and authority over the client" (Haug 1973:197).

Deprofessionalization focuses on a variety of social, economic, and political changes that "have combined to significantly alter the environment that facilitated the emergence and dominance of the modern knowledge-based professions" (Rothman 1987:83). Sociologists document the

significance of environmental changes on deprofessionalization within a number of professions (see Reeder 1972; Haug 1975; Rothman 1987). Relevant environmental factors include erosion of professional knowledge monopoly, decreasing trust in professional judgment, technological change, and encroachment from allied professions (Haug 1975; Rothman 1984).

STATEMENT OF THE PROBLEM

This study seeks to answer the question: Why was there variation among firms in deprofessionalization of stockbrokers in the United States during the period 1975 through 1990? The study attempts to determine what effect, if any, differences in responses of brokerage firms to environmental changes had on variation among firms in deprofessionalization of stockbrokers. During the period in question there were three primary environmental factors that necessitated organizational response: changes in jurisdictional competition, changes in technology, and changes in public trust in professional judgment. For this project, these environmental factors are investigated in industry specific terms: banking deregulation, computerized trading and information services, and widespread scandals within the brokerage industry.

The time period from January 1, 1975 to December 31, 1990 has been chosen for this study because it was a time of

extensive change in all three of the environmental factors being considered. The end of fixed commission rates in May 1975 indicates the beginning of a deregulation process in the financial marketplace that continued through the 1980s. This period also included numerous changes in technology, as well as numerous revelations of unethical and illegal behavior leading to numerous scandals in the brokerage industry.

It could be argued that behavior leading to scandals was caused by economic conditions resulting from increased competition created by deregulation. However, studies to test the relationship of declining profitability and corporate crime have found only modest support (Clinard et al. 1979; Staw and Szawajkowski 1975). A recent longitudinal study of economic and criminal activity (Simpson 1986) found that only certain forms of criminality are related to profit-squeeze, others are unrelated to economic conditions, while some occur within munificent environments. It is beyond the scope of this study to consider precise time ordering of deregulation, changing technology, and scandals. The study will consider these factors as interrelated environmental changes that were likely to elicit differing organizational responses, which in turn would effect variation in deprofessionalization.

Since much of the available information concerning the securities industry between 1975 and 1990 can be found in

business periodicals, I have utilized content analysis for this study. Three firms with responses that appear to be different have been selected for comparison. In addition to quantitative content analysis to determine differences in organizational responses, qualitative analysis is used to examine variation among firms in deprofessionalization as a result of differences in organizational responses to bank deregulation, changes in technology, and widespread scandals.

SIGNIFICANCE OF THE PROBLEM

Deprofessionalizatiton takes place in a context that helps determine the extent of change (Abbott 1988:23). Organizational responses to changes in the environment are an important part of this context. Strategies that are adopted by an organization have widespread consequences, and professionals are not exempt from these consequences.

By using strategic choice theory, developed by industrial relations scholars, this project links two areas of deprofessionalization research, i.e., the effects of environmental changes and the effects of organizational employment of professionals. Strategic choice theory recognizes the relevance of environmental changes, but asserts that these changes do not exert a deterministic force. Instead, firms frequently respond differently to the same environment. Scholars use strategic choice theory to

assess the influence of strategic organizational decisions on groups and individuals at all levels of the organization (e.g. Kochan, Katz, and McKersie 1986, 1991; Kochan, McKersie, and Cappelli 1984).

The literature on deprofessionalization, which is discussed in Chapter Two, suggests that professionals lose their identifying traits and/or their power as they become a part of a large organization. The content of their work and their control over their work often change. Decisions concerning professionals and their work are taken out of the hands of those within their own profession, and increasingly placed in the hands of corporate managers and executives. As the number of professionals employed by organizations has increased, the possible effects of organizational employment on professionals has become a significant part of the study of deprofessionalization.

However, one aspect of organizational employment of professionals that has not been explored is the effect that organizational responses to environmental changes have on deprofessionalization. Deprofessionalization research has not addressed firm-level strategies and their influence on professionals, and strategic choice theory has not addressed the influence of particular strategies on the professionals within an organization.

In the years 1975 through 1990, environmental factors affecting the securities industry in the United States

included not only the competitive shock of deregulation, but also changes in technology and widespread scandals. This study uses a comparison of three brokerage firms to determine differences in organizational responses to these environmental changes, and whether or not the responses mediated the effects of the environmental changes on deprofessionalization. The exploration of differences in organizational responses in an industry experiencing rapid change can contribute to the understanding of how organizational responses affect variation in deprofessionalization.

RESEARCH QUESTIONS

Four research questions serve to guide the development and implementation of the study:

1 - In the period 1975-1990, how did brokerage firms differ in their response to bank deregulation?

2 - In the period 1975-1990, how did brokerage firms differ in their response to changes in technology?

3 - In the period 1975-1990, how did brokerage firms differ in their response to scandals within the industry?

4 - How did differences in organizational responses affect variation among firms in deprofessionalization of stockbrokers?

CHAPTER 2

REVIEW OF LITERATURE

In order to address the issues involved in the variation of deprofessionalization of stockbrokers in the United States from 1975 through 1990, I have reviewed several types of literature. Literature on professionalization provides a foundation for this study. Deprofessionalization, a systems theory of professions, and strategic choice theory constitute the theoretical basis for this project. I have examined literature pertaining to jurisdictional competition, changing technology and declining trust, since these are the environmental changes being considered. These environmental changes are reviewed in general terms, as well as ways in which they specifically relate to the deprofessionalization of stockbrokers. In keeping with the organizational focus of the study, I have also reviewed literature on organizational employment of professionals.

PROFESSIONALIZATION

For most of the twentieth century sociologists have had an intense interest in professions. There have been

numerous and diverse efforts to explain precisely what a profession is and how an occupation becomes a profession. Freidson notes, the "occupations to which the word has been applied are so varied as to have nothing in common save a hunger for prestige" (1970:4).

Some scholars (e.g. Reiss 1955; Goode 1960; Etzioni 1969; Forsyth and Danisiewicz 1985) identify degrees of professions rather than a simple dichotomy between nonprofessions and professions. Professions are classified using terms such as true professions, old established professions, new professions, would-be professions, marginal professions, semiprofessions and mimic professions. Although there is no general agreement on terminology, most occupational sociologists agree that occupations exist along a continuum ranging from nonprofessions to established professions (Ritzer and Walczak 1986:61).

Trait Perspective

Structural-functional or trait theory (e.g. Greenwood 1957; Goode 1957, 1960) views professions as occupations that are worthy of special recognition because they require more skill and dedication than other occupations. The relationship between professions and society is seen as an exchange, with society providing autonomy in return for the profession's development of specialized knowledge. Higher income and prestige are seen as "logical" rewards for well trained and highly motivated professionals (Begun 1986:114).

Trait scholars emphasize a set of characteristics that identify a profession. They argue that these characteristics are "real" qualities possessed by professions, but lacking in nonprofessions. Basic concepts of this theory can be seen by looking at the six most frequently cited professional characteristics (Ritzer and Walczak 1986:70-78).

1) General systematic knowledge. Professions are identified by their general systematic knowledge that is transmitted through a lengthy professional training program. This knowledge base is viewed as complex and as important to society.

2) Norm of autonomy. Professions are identified by their freedom from external social control concerning judgments and behavior. It is assumed that external interference would reduce the quality of professional service.

3) Norm of altruism. Professions are identified by their altruism or community interest in contrast to the self-interest of other occupations.

4) Norm of authority over clients. Professionals are seen as having authority over clients. It is also assumed that "a questioning clientele would reduce the quality of their service" (Ritzer and Walczak 1986:76).

5) Distinctive occupational culture. Those in professions claim to have a distinctive occupational culture that differentiates professions from nonprofessional occupations.

This culture is developed through formal organizations such as professional associations and training schools, as well as through informal groupings within the profession.

6) Recognition by community and law. The community and the law recognize formally and/or informally that professions possess the five traits listed above. Formal recognition usually includes licensing of a profession.

The identification of an occupation as a profession by the presence of these key traits or characteristics is central in this view of professions. Although there is recognition that the traits vary in their intensity, they are used to determine whether or not an occupation is a profession. Nonprofessions are thought to have few, if any, of these characteristics (Ritzer and Walczak 1986:70).

Overall, the structural-functionalist explanation of "essential" traits of "true" professions includes many inconsistencies and differing terminology (Klegon 1978:262). Although some traits are considered essential, there is no clear agreement on the list of essential traits. Roth (1974) notes that unique attributes of professions listed by the same author may vary at different times, and that these attributes are "largely mixtures of unproved--indeed, unexamined--claims for professional control and autonomy" (1974:7).

Another problem with this theory is the difficulty of applying the characteristics to concrete situations. For

example, Wilensky (1964) describes the knowledge base of a profession as "neither too vague nor too precise, too broad nor too narrow" (1964:148). Accurate application of this criteria to a specific occupation would be virtually impossible. In spite of rigid definitions of professions and difficulties in application, the characteristics developed by this perspective are useful in a general understanding of professions. These characteristics are important in a study of deprofessionalization since the concept of deprofessionalization is based on the loss of these distinctive characteristics. On the other hand, it focuses on structure rather than on professional tasks, which limits its usefulness for this project. Because of the previously innumerated limitations, trait perspective falls short of a realistic representation of professions. One of the critical problems of trait perspective for this study is its failure to address change in professions, which is a primary focus of this study.

Process Perspective

The process approach looks beyond the existing structure of professions, as exemplified in professional characteristics, to the historical development of that structure. The process perspective (e.g. Caplow 1954; Hughes 1958; Wilensky 1964; Vollmer and Mills 1966) identifies a series of steps in the professionalization process. Scholars differ in their identification of the

steps and their sequence, as well as in ideas of the concreteness or universality of the sequence (e.g. Caplow 1954; Millerson 1964; Wilensky 1964). Wilensky's sequence is one that is often used: 1) substantial number of people doing needed service full time; 2) setting up training school; 3) professional organization; 4) efforts to win legal support; 5) code of ethics (1964:142-145).

In keeping with their emphasis on the dynamic process of professionalization as a key element in understanding professions, scholars using the process perspective look at the extent to which an occupation has moved through particular steps (Vollmer and Mills 1966). The focus is not only on the structure of a profession, but on the evolution of that structure. Professions display diverse properties, and the process perspective attempts to explain this diversity by showing that some occupations have not finished the process of professionalization (Abbott 1988:15). Focus is placed on the extent to which an occupation is a profession, judged by location within a process that follows a characteristic order.

Wilensky (1964) concludes from his analysis of the process of professionalization that certain events follow the same precise order in each profession. However, results of empirical research by Abbott (1991), while showing some regularity in medical professionalization, more importantly show professionalization as a complex process

with considerable variation at local, state and national levels. Abbott's conclusion was that the professionalization process is a "multilevel, contagious, complex social process...not a simple collective action by a cohesive group" (1991:380).

Power Perspective

During the early part of this century, trait and process views dominated the sociological study of professions. However, these theories were generated in a period of relative stability for professions. Trait theory's unchanging list of essential traits is difficult to apply in periods of rapid change, and the orderly process of development described by process theorists is more likely during times when areas of work are uncontested.

In the 1970s critics of these theories proposed an alternative perspective, identified as the power model (e.g. Freidson 1973; Roth 1974; Klegon 1978; Ritzer and Walczak 1986). In general, the power perspective rejects the premise that professions are distinguished by inherent characteristics or by distinctive historical stages. Power theorists believe that process and trait theories underestimate the significance of the political process and the importance of professional power.

According to the power model, the traits enumerated as identifications of professional standing are not important in themselves, but are important only in relationship to the

power that makes them possible. The power perspective sees professions as "occupations that had the power...to win the exalted label of 'profession' and once they did, they were seen as exploiting that situation to further enhance their power" (Ritzer and Walczak 1988:5).

Ritzer and Walczak suggest that the power perspective can be better understood through a critique of the six professional characteristics identified by structural-functionalists (1986:70-78).

1) General, systematic knowledge. Power theorists argue that many nonprofessional occupations have a knowledge base, and that professions must rely on information from various sources outside their profession. Power advocates assert that there are no real qualitative differences in nonprofessional and professional knowledge, but that professions attempt to create the illusion of distinctive knowledge.

2) Norm of autonomy. The power approach points out incidences of external control in the history of all professions. The history of professions also fails to support the belief that professional autonomy contributes to high standards of service (Daniels 1973:55).

3) Norm of altruism. Power advocates argue that the service ethic of professions "is a myth created and perpetuated to enhance their status" (Ritzer and Walczak 1986:74), and to "silence the critics of monopoly,

privilege, and power to which professions are attempting to cling" (Halmos 1973:6). Through this myth, professions attempt to convince the public that they are not self-interested, and can therefore be trusted to operate according to altruistic principles.

4) Norm of authority over clients. The power perspective asks whether or not uncontested authority ever existed, and goes a step further to ask if professions need unquestioned authority. Power advocates propose that a questioning clientele is more likely to move a profession toward a higher level of performance, rather than a lower level (Ritzer and Walczak 1986:75).

5) A distinctive occupational culture. Power advocates see professional cultures as simply more elaborate, rather than qualitatively different from other occupational cultures. The "professional culture simply has more of everything, most notably more power" (Ritzer and Walczak 1986:78).

6) Recognition by community and law. Power theorists see all of the myths of the previous characteristics aimed at attaining this recognition. The power perspective asserts that "a profession may not really possess these traits; it may simply have the power to convince the public, the law, and other sectors that it possesses them" (Ritzer and Walczak 1986:70).

In extreme form, the power perspective is based on the assumption that the only qualitative difference between

professions and nonprofessions is the greater power possessed by professions (McKinlay 1973: 67). This power includes authority over clients, autonomy from employing organization, and power to close professional jurisdictions to outsiders (Abbott 1991; Forsyth and Danisiewicz 1985). A less extreme view argues that identifying characteristics of professions are derived from either the power to create the traits or the power to convince others that they possess the traits (Ritzer and Walczak 1986:80).

Historically, sociologists have used these three views--trait, process, or power--to understand professions and the process of professionalization. This overview of professionalization theories provides a foundation for the study. These theories have been reviewed because each of them includes aspects relevant to this project. Trait theory innumerates distinctive characteristics of professions that form the basis for an understanding of deprofessionalization. The process perspective goes beyond the structural emphasis of trait theory to address the process of professional development. The power view emphasizes professional power, including the power to exclude outsiders from professional jurisdictions. However, these views also have some serious limitations. Therefore, the following sections will review areas more directly related to this project, including deprofessionalization,

systems theory, strategic choice theory, and environmental factors influencing deprofessionalization.

DEPROFESSIONALIZATION

It was once assumed that professions did not lose status (Goode 1960). The term professionalization implies change in only one direction, but Abbott (1988; 1991) provides theoretical arguments and empirical evidence that professions do not move in a single direction. Deprofessionalization is that process of decreasing or eliminating the characteristics that identify an occupational group as a profession (Hodson and Sullivan 1990:275). Research identifies changes indicating deprofessionalization occurring in numerous professions, including medicine (Reeder 1972; Marsden 1977; Ritzer and Walczak 1988), law (Rothman 1984; Anleu 1992), and pharmacy (Toren 1975).

Power theorists see the process of deprofesssionalization as a sign of the veracity of their view, since it provides a critique of the trait view of professions. The process of deprofessionalization indicates that the traits considered to identify professions are not undeniable, irrefutable characteristics which grow out of the importance of the function performed, but are subject to change as economic, political and social changes create shifts in power. It also suggests that power is fragile (Ritzer and

Walczak 1988). Society (Jamous and Peloille 1970), other occupations (Zola and Miller 1973; Larkin 1983), or clients (Rothstein 1973) can bestow power, but can also limit or withdraw power, which means that professions must work constantly to protect that power.

Haug (1973, 1975) was one of the first to analyze the process of deprofessionalization. Haug defines deprofessionalization as "the professional occupations' loss of their unique qualities, particularly their monopoly over knowledge, public belief in their service ethos, and expectations of work autonomy and authority over client" (1973:2). She asserts that a number of economic, political, and social changes are bringing about the process of deprofessionalization. These changes occur within the larger society rather than within specific professions, and are thus referred to as environmental changes.

The environmental changes mentioned most often by Haug and others (e.g. Haug 1973, 1975; Toren 1975; Rothman 1984; Ritzer and Walczak 1988) include: narrowing of the competence gap, routinization of expert knowledge, encroachment by allied professions, organizational employment, increasing control by outsiders, declining client trust in professional authority, and changes in technology. These changes in the environment form a complex web of influence on professions.

For example, a competence gap between professionals and clients was one of the environmental factors that helped to develop and maintain the concept of professional authority and expertise. Unquestioning trust in the knowledge and authority of professionals was more likely in a period when this knowledge was the exclusive domain of professionals, and the educational level of the population was relatively low (Rothman 1987:83).

A narrowing of the competence gap between professionals and clients has resulted from a rising level of education in the population of the United States. A better educated clientele is more likely to question the authority of professionals. A more sophisticated clientele is likely to recognize that some services that were once thought to require professional expertise are now routine. So rather than consulting a lawyer, individuals might prepare their own will or residential property transfer by using a "do-it-yourself" legal manual or computer software (Rothman 1987:84). A clientele with more information available through education and mass media are more likely to seek a second opinion, make active demands about the conduct of their cases, (Rosenthal 1974:31), initiate suits, or participate in consumer groups to bring about legal changes (Rothman 1987:87).

A key issue in deprofessionalization literature is the recognition that professional status, authority, and

autonomy can be lost as well as gained. Social, political and economic changes constitute environmental factors that bring about these losses. The effect of changes in the environment on deprofessionalization has been considered to be a direct effect. However, strategic choice theory, discussed later in this chapter, suggests that for professionals in organizations, this effect is mediated by organizational responses to environmental factors.

SYSTEMS PERSPECTIVE

Abbott (1988) suggests a systems perspective for the study of professions. This theory incorporates both professionalization and deprofessionalization through its emphasis on multidirectional change. Systems theory views professions as a system of interrelationships, with each profession having its own particular areas of work or activity. Because jurisdictions are exclusive, a move across jurisdictional boundaries by one profession inevitably affects other professions. Interrelationships shift as professional groups vie for control of knowledge and power by redefining their problems and tasks, by defending their jurisdictions from intrusion by others, and by expanding their areas of problems and tasks. Systems theory does not deny the importance of power, but defines professional power as the "ability to retain jurisdiction when system forces imply that a profession ought to have

lost it" (Abbott 1988:136). This theory accounts for changes in professional groups, including deprofessionalization, through redefinition of problems and expansion or narrowing of tasks.

A strong focus on work is a key element of this theory. Rather than addressing professionalization and deprofessionalization only in terms of shifts in power and prestige, systems theory looks at shifts in daily activity. Emphasis is placed on the content of work and control of work, which are generally recognized as important differences in professions and other occupations.

Abbott asserts:

> The central problem with the current concept of professionalization is its focus on structure rather than work. It is the content of the professions' work that the case studies tell us is changing. It is control of work that brings the professions into conflict with each other and makes their histories interdependent. It is differentiation in types of work that often leads to serious differentiation within the professions (1988:19).

Abbott (1988:17) maintains that various views from trait and process theories can be synthesized into a general concept of professionalization that includes five erroneous assumptions:

1) Change is unidirectional.
2) Evolution of individual professions is not dependent on that of others.

3) Social structure and cultural claims are more important than the work professions do.

4) Professions are homogeneous units.

5) The process of professionalization does not change over time.

He argues that systems theory reverses these "problematic" assumptions.

Professions cannot be adequately explained as static independent units, instead in systems theory there is an emphasis on multidirectional change within professions, and interaction within a system of professions. The jurisdiction of a profession is the link between the profession and its work, but this link is not permanent or absolute. Changes in professions generally start with some kind of disturbance followed by jurisdictional contests resulting in changes or adjustments. These elements are important in my examination of the profession of stockbrokers during a period of rapid environmental change and increasing jurisdictional competition.

The systems model proposed by Abbott not only provides a clear explanation of multidirectional changes in professions, but is widely applicable over various professions and is useful in times of rapid societal, technological, and economic change. The position taken in this study follows that of Abbott in that changes in content and control of work are considered important elements in

understanding deprofessionalization. Professions are seen as interrelated groups who defend their spheres of activities, or jurisdictions, seek to expand their jurisdictions and intrude on the jurisdictions of others. A systems approach to studying professions focuses on the content and control of work, on forces for change, and on jurisdictional competition among professions, all of which are vital aspects of this study.

Although systems theory provides the theoretical foundation for this study, it is used in conjunction with strategic choice theory. Systems theory explains ways in which changes in professions are influenced by external social forces or environmental changes. Strategic choice theory goes a step further by explaining how the effects of external social forces are mediated by strategic choices within organizations. Strategic choice theory comes from industrial relations literature rather than professionalization literature. However, it is applicable to professionals in organizations because organizational responses to environmental changes affect all levels of an organization. When considering how environmental changes influence deprofessionalization, the mediating effects of organizational responses also need to be considered.

STRATEGIC CHOICE THEORY

In 1984 Kochan, McKersie, and Cappelli published a paper containing preliminary results of a three-year research project. The stated purpose of this paper was "to add a more dynamic component to industrial relations theory by developing the concept of strategy, or strategic choice" (1984:16). This theory was later presented in greater detail in <u>The Transformation of American Industrial Relations</u> (Kochan, Katz and McKersie 1986).

The theoretical framework of strategic choice is based on the "key premise that industrial relations processes and outcomes are determined by a continuously evolving interaction of environmental pressures and organizational responses" (Kochan, Katz, and McKersie 1986:13). Although the specifics of application differ in industrial relations and professions, this premise of interaction of external environment and organizational response is applicable in both areas.

Developed during the 1980s, a period of intensified competition and technological change, the theory argues that effects from these external forces are mediated by business strategies. There are no inevitable consequences of environmental change because firms "often respond differently to the same environment" (Kochan, Katz, and McKersie 1991:105). Environmental changes may occur gradually, but in some cases these changes are abrupt, as

indicated by the deregulation of banking, airlines, and trucking industries.

The strategies used in response to changes in the competitive environment are particularly pertinent for this study. These include cost reduction, quality improvement, innovation, and seeking out specialized market niches (Schuler, Galante, and Jackson 1987:18; Kochan, Katz, and McKersie 1991:108). Firms that respond to increased competition by using a cost-reduction strategy are often able to keep prices down by minimizing overhead and lowering labor costs. Companies using low cost strategy do not require employees with significant commitment to the job, but instead are more likely to value high concern for quantity and predictable, repetitive behavior (Schuler, Galante, and Jackson 1987:23). Strategic choice theory argues that, in general, "the stronger the position of labor in the firm the less likely it will be that the low cost strategy will be adopted, and if adopted, the more conflict that will result" (Kochan, Katz, and McKersie 1991:109). Relating the proposition to this project, it would also seem that the stronger the position of professionals in a firm, the less likelihood there would be of adoption of a low cost strategy.

Financial resources of the firm may limit or expand options in choosing competitive strategies. In studying competitive pressures on the airline industry as a result of

deregulation, Cappelli (1985:323) grouped carriers according to options open to them. He found that a "strong" group had sufficient financial resources to restructure their operations to meet competitive pressures. A "vulnerable" group had lost tremendous amounts of money and had fewer options and less potential for growth. A "near bankruptcy" group was even weaker financially and used short-term strategies in attempting to avoid bankruptcy. The context in which strategies are chosen includes, but is not limited to, financial resources. While financial resources cannot predict choices, they may limit available options.

Kochan, McKersie, and Cappelli (1984) suggest that by looking at a single industry over time, "it is possible to illustrate more clearly the proposition that firms facing the <u>same</u> environmental changes may vary in their business strategy responses" (1984:31). They examined variations in corporate responses in the tire industry. In this study I examine differences within the securities industry.

ENVIRONMENTAL FACTORS
INFLUENCING DEPROFESSIONALIZATION

Deprofessionalization is influenced by a wide variety of social and economic factors. For this project I have chosen three environmental changes that have been linked to deprofessionlization. Research indicates that these changes in the environment--jurisdictional competition, changing

technology, and declining client trust--affect deprofessionaliztion (e.g. Haug 1975, 1977; Toren 1975; Betz and O'Connell 1983; Ritzer and Walczak 1986, 1988).

Jurisdictional Competition

Encroachment from allied professions has long been recognized as a factor in the deprofessionalization process (Haug 1975:206). When jurisdictional boundaries are disrupted, new competitive situations often result. Abbott (1988) refers, instead, to jurisdictional competition. This terminology avoids the unidirectionality implied in "encroachment from allied professions". Abbott argues that movement across broken jurisdictional borders is often multidirectional.

An example of this multidirectional movement is seen in the profession of psychiatry, which emerged in the nineteenth century to challenge the legal profession in dealing with mental illness. Until the late nineteenth century the profession of psychiatry was associated almost exclusively with administration of mental institutions. However, in the early twentieth century psychiatry sought to expand into new areas by providing treatment in cases of juvenile delinquency, alcoholism, and marital strife. This brought them into conflict with the clergy, the law, psychology, and social work.

Psychiatrists seemed to be the winners in these conflicts, because they continued to dominate the

jurisdictions they had seized until the 1970s. The increased demand for psychotherapy during that period brought psychologists and social workers into areas previously protected by psychiatry (Abbott 1988:23). For example, by the 1980s much treatment for alcoholism was taking place in treatment centers. Treatment center personnel included not only psychiatrists, but other professionals, such as psychologists and social workers.

This example indicates that once the clarity of professional borders is disrupted, there is the possibility of considerable movement across those borders in the process of jurisdictional competition. Psychiatry has clearly maintained much strength as a profession. Psychiatrists remain the only mental health professionals who are able to prescribe medications and hospitalize patients. In a setting that includes other mental health professionals, psychiatrists are likely to supervise and direct the actions of others. However, since maintaining jurisdictions and expanding into new areas are usually seen in positive terms, systems theory suggests that the inability of psychiatrists to maintain their jurisdiction unscathed is an indication of deprofessionalization.

Psychiatry is only one of many examples of jurisdictional competition. The legal profession has a long history of jurisdictional competition with professionals who perform work relating to the law, such as accountants,

bankers, tax consultants, and realtors. Although the legal profession has remained dominant, other professions have made inroads into legal jurisdictions. Realtors in Arizona now have the right to draft property transfer documents (Christensen 1980:199), and title insurers in Virginia have the right to make title searches (Rothman 1984:196).

In the field of health care, optometrists, pharmacists, and other health care professionals have sought to move into protected jurisdictions of established professions and have sometimes been successful. In recent years a number of states have granted optometrists the right to expand their jurisdictional boundaries to include the application of drugs to the eye. By 1982, thirty-two states allowed optometrists to use diagnostic drugs, while other states also allowed use of drugs for therapeutic purposes. This expansion was an intrusion into the profession of ophthalmology (Begun and Lippincott 1987:369). In 1986 pharmacists in Florida encroached on the monopoly of physicians by gaining the right to prescribe thirty different medicines for treatment of minor illnesses (Rothman 1987:88).

Sometimes rather than being directly initiated by an allied profession, changes in jurisdictional boundaries begin with changes in government policies or regulations. Once the jurisdictional boundary is weakened, other professions then move into the vulnerable area. This was

the situation for stockbrokers in 1975 when a Securities and Exchange Commission (SEC) ruling proved to be the first in a chain of events that seriously weakened the previously protected jurisdiction of stockbrokers.

Jurisdictional Competition and Deprofessionalization of Stockbrokers

For the securities industry, jurisdictional disruption and subsequent deprofessionalization of stockbrokers resulted, in part, from banking deregulation. The competitive environment, brought about by removal of the barriers between depository and nondepository financial institutions led to a great deal of movement across previously protected jurisdictional boundaries.

Banking regulation in the United States was enforced primarily through the Banking Act of 1933, which was enacted in response the the 1929 market crash and the depression that followed. This act, which later came to be known as the Glass-Steagall Act, included a number of restrictions which separated commercial banking from investment banking. Clear guidelines were established for banks and for securities firms; thus, the two were separated by the Glass-Steagall Wall (Khoury 1990:54). Within the brokerage industry this regulatory separation is referred to as the Chinese Wall because of its apparent strength and durability.

The first crack in the Glass-Steagall Wall came in 1975 from an unexpected source. For almost two hundred years the stock exchanges had fixed the commission rates for all members. The May 1975 ruling by the Securities Exchange Commission (SEC) that the exchanges could no longer require members to adhere to fixed commission rates ended the country's oldest legal monopoly (Coler 1989:13). Although most brokers continued to charge the same rate, the SEC decision opened the door for the formation of discount brokerage firms. By the early 1980s, banks also began to offer discount brokerage services. A 1984 survey showed over three thousand banks offering discount brokerage services of one form or another (Coler 1989:14).

In the 1980s additional cracks appeared in the Glass-Steagall Wall through court rulings and decisions of the Federal Reserve Board. The Federal Reserve Board in 1983 allowed the acquisition of the Charles Schwab discount brokerage firm by the BankAmerica Corporation, a decision that was later upheld by the Supreme Court. In January 1986 the Supreme Court upheld rights of national banks to offer discount brokerage services, followed the next year by a ruling that allowed national banks to establish interstate brokerage branches. This ruling made possible the development of nationwide securities businesses by banks (Khoury 1990:57). Allied professions had thus made inroads into stockbrokers' jurisdiction and the movement was

facilitated by regulatory changes. Within the space of a few years the sturdy Chinese Wall had begun to crumble.

The brokerage firm side of the Glass-Steagall Wall was also being broken down. In the 1970s brokerage firms such as Merrill Lynch and American Express began offering money market funds. Brokerage firms had an advantageous position because they were able to offer customers higher rates of interest than banks. Differences in interest rates offered by banks and brokerage firms in the 1970s were the result of legislation passed in 1935 to avoid what was considered destructive competition among banks. This legislation, known as Regulation Q, limited interest rates that could be paid by depository institutions (Pierce 1984:288). However, nondepository institutions were not subject to Federal Reserve Regulation Q, under which the Federal Reserve set interest rate ceilings.

Therefore, brokerage firms were able to offer a market rate of interest to the small saver at a time when rates at depository financial institutions were limited by law. These money market accounts not only offered clients better interest rates, but made it possible to keep money in-house between stock or bond trades, which was advantageous to brokerage firms. A 1982 study revealed that some securities dealers, in addition to their traditional financial services such as selling stocks and bonds, were also offering

checking, saving, time deposits, installment, business and mortgage loans, and credit cards (Cooper and Fraser 1989:5).

By the end of the 1980s the Glass-Steagall Wall separating depository financial institutions from brokerage firms had been significantly attacked from both sides. There was a definite blurring or overlapping of functions in the financial marketplace. These changes in the role of financial institutions brought increased competition to brokerage firms as they saw both discount brokerage firms and banks move into their previously protected financial marketplace. As a result of boundary disruptions and the jurisdictional competition that followed, the likelihood of deprofessionalization of stockbrokers increased.

Changes in Technology

There are two primary ways in which changes in technology have led to deprofessionalization. Both represent a loss of control over knowledge and negation of professional claims of authority and expertise.

First, control over knowledge is lost when professionals are dependent on technology and/or the knowledge of others in making professional judgments. For example, physicians seldom base diagnostic judgments on their own observations of patients. Instead, diagnoses are developed primarily from technicians' interpretation of complex medical technologies (Ritzer and Walczak 1988:12). Physicians usually give the information to patients, but

patients' awareness that the knowledge comes from technologies and technicians erodes physicians' authority.

A second loss of control over knowledge comes from professional knowledge becoming routine. Widespread availability of computers, along with increasingly complex software, has revolutionized the availability and the utilization of knowledge in many professions. Specialized knowledge, on which professional expertise is based, is no longer as inaccessible to those outside the profession as it was in the past (see Toren 1975; Haug 1975, 1977; Ritzer and Walczak 1988; Farrell and Light 1990). Haug (1975:205) points out that control of stored knowledge depends less on whether one knows it and more on whether one knows how to retrieve it. This standardization and routinization of expert knowledge brought about by technological innovation is considered to be one of the primary sources of deprofessionalization (Toren 1975:329).

The most dramatic example of the impact of technology on professions is that experienced by the medical profession (Haug 1977). Not only did physicians find themselves dependent on sophisticated medical technology, but in many cases the challenge to authority and autonomy go even further when patients are able to bypass the physician altogether, as seen in home pregnancy tests, blood pressure monitors and other tests which are available to the patient (Ritzer and Walczak 1988:13).

Although the legal profession has been affected less dramatically than the medical profession by changing technology, there has been an increase in computerized research facilities and record keeping, particularly in large law firms (Anleau 1992:189). Computers are used for a variety of tasks including drafting legislation, screening prospective jurors, and researching legal precedents (Haug 1977:219). The full text of federal and state legislation, along with Supreme Court decisions, are now on disc storage. They are indexed and quickly retrievable (Rothman 1984:191).

When a person outside the legal profession has access to the full text of Supreme Court decisions, or a person outside the medical profession can perform a pregnancy test, then to some extent these professions have been "stripped of their magic elements" (Toren 1975:330). Therefore, changes in technology have been a source of deprofessionalization by eroding professional claims of complex work requiring expert knowledge.

Changes in Technology and Deprofessionalization of Stockbrokers

Within the securities industry, technical changes in the past two decades have changed the profession of stockbroker and increased the likelihood of deprofessionalization. Complex computer assisted trading techniques have radically changed the speed of stock trading. At the same time, computers have changed the daily

lives of stockbrokers in terms of acquisition of market information and analysis, as well as ways in which customer accounts are handled.

When the New York Stock Exchange introduced the Designated Order Turnaround system (DOT) in March 1976, it was intended to "alleviate the burden of handling small retail market orders" (Dunn 1989:178). The system executes small orders electronically at prevailing market prices. DOT was followed by Super DOT which made possible a cost-efficient way to execute a large cross-section of stocks at once (Dunn 1989:179). Electronic trading networks and order-matching systems continue to grow in speed and scope.

Before trading and execution of orders was done electronically, there was a great deal of human involvement. Orders were usually given to a broker in person or over the telephone, trading tickets written manually and given to a "wire operator", who transmitted them to the exchange by teletype. On the exchange floor tickets were written and taken to the appropriate trading post, where the trader would make the actual trade.

With changes in technology an order may start by being transmitted from customer to broker by computer, particularly if it is for a list of stocks. Once the order is stored in the memory of the broker's computer, the list can be screened in ways that give pre-trade information, which result in a better execution. Orders are then

transferred by computer to the exchange floor and routed to the appropriate trading post electronically. No tickets need to be written and execution takes place much more quickly (Spehar 1989:163).

While electronic systems were changing trading at the market level, computers were also changing the daily life of the stockbroker. It was no longer necessary to depend on customer notebooks or monthly statements for information concerning transactions or stocks held in an account. It was no longer necessary to depend on stock publications or a telephone call to an analyst to ascertain performance of a particular stock. A computer terminal on his/her desk gives the broker vast amounts of product and customer account information.

However, while advanced technology was providing information for brokers, it was also making information more accessible to clients (Wall Street Journal Feb. 27, 1985:20). Widely available computer hardware and software made once exclusive market information available to anyone with a computer terminal. A 1984 book on stock trading software (Packer) promised: "the analysis of individual investment situations on desktop micros will soon be a commonplace service to millions of small investors" (1984:ix). This promise is backed up by a list of 143 relevant software programs. This wider accessibility of

financial knowledge led to increased deprofessionalization for stockbrokers.

Declining Trust

Declining trust has been frequently noted as a key element in the deprofessionalization process (e.g. Reeder 1972; Haug 1975, 1988; Burnham 1982; Betz and O'Connell 1983). One of the factors linked to the erosion of trust is a narrowing of the competence gap (Parsons 1970), or narrowing of the difference in the educational level of professionals and the average educational attainment of the population (Haug 1975). Higher levels of education often lead to increased sophistication about professional expertise as well as greater skepticism concerning professionals and their work (Wilensky 1964:150). Increased education and public awareness has made it more difficult for professionals to demand and receive unquestioning trust and passive acceptance of professional judgment (Rothman 1984:84).

Another factor in declining trust is consumerism, a broadly based social movement with beginnings generally traced to the 1960s. "Individual consumers, consumer groups, state legislatures, and the federal government began to scrutinize the professions and challenge traditional prerogatives" (Rothman 1984:194). Opposition of the American Medical Association to national health insurance in the face of enormous health care problems of the poor,

opposition of the legal profession to "no-fault" auto insurance at a time of increasing repair costs, and large malpractice settlements (Rothman 1984:87) stimulated public awareness of a need for closer scrutiny of professional performance. There has been a call for public accountability of professionals, which implies that "the image of the professional as kindly, concerned and trustworthy is no longer widely shared" (Haug 1975:206).

In the medical profession there has been a move from unquestioning obedience of patients to actions varying from demand for participation in decision making to malpractice suits (Haug 1988:53). Within the past twenty-five years, but especially in the last ten years, physicians have found "their prestige reduced and their competence challenged by everyone from oversight boards to hostile, litigious patients" (Altman and Rosenthal 1989:1).

In both the medical and legal professions erosion of trust has been linked to an increase in specialization. The increase in malpractice litigation reflects a growing impersonality of doctor-patient relationships. This type of relationship is more likely in a specialist-patient situation, because the narrow range of symptoms dealt with by a specialist increases the tendency to be concerned with disease rather than with people (Betz and O'Connell 1983). Studies of the legal profession also suggest specialization as a factor in fragmented relationships with clients, which

makes distrust more likely (see Nelson 1981, 1988; Heinz and Laumann 1982; Anleu 1992).

In the case of the professional-client relationship, trust can be defined as a "social relationship in which principals...invest resources, authority, or responsibility in another to act on their behalf for some uncertain future return" (Shapiro 1987:626). However, recent literature on trust suggests that not only has there been a decline of trust in the professional-client relationship, but that the nature of the trust has changed (e.g. Granovetter 1973, Shapiro 1987, Fombrun and Shanley 1990). In times of shifts in management and mergers that increase corporate size, trust becomes more impersonal. This impersonal trust develops when relationships are transient rather than continuing, and when relationships are not embedded in networks of social relations (Shapiro 1987:635).

For professionals who represent large corporations, perceptions of the trustworthiness of a professional in an organization are linked to some extent to the perceived trustworthiness of the organization. Individuals rarely have the time or expertise to gather the data necessary for a judgment of trustworthiness (Shapiro 1987:627). Therefore, they judge the reputation of a firm based on information from the firm itself and from representations of the news media (Shapiro 1987; Fombrun and Shanley 1990). In an empirical study of 292 large U. S. firms, Fombrun and

Shanley (1990) found that the public constructs reputations of firms by using a variety of signals: 1) marketing and accounting signals such as stock price and reports of economic performance 2) institutional signals, which include social responsibility and mass media presentation, and 3) strategy signals concerning outcomes of corporate strategies(1990:252-253).

Declining Trust
and Deprofessionalization of Stockbrokers

Although the financial services industry has never been known for its altruism, it has historically operated on the assumption that providing honest and dependable client services was a vital key to long-term success (Morton 1989; Wagner 1989). Henry Clews (1973), writing in 1908, tells of the personal honor of Wall Street men: "There is no place in the world where people are trusted so much on faith as they are in Wall Street; not even in the Church" (1973:33). Clews, a Wall Street man himself, may have overstated the case, but evidence suggests that many stockbrokers have earned the respect and trust of their clients (e.g. Stone 1975; Auerbach and Hayes 1986; Morton 1989).

In spite of Clews' declaration of unwaivering trust in "Wall Street men", client trust of stockbrokers has waivered considerably over the years. In the nineteenth century there were accusations of "error, fraud, and theft" (Stone

1975:28). The decline in trust as a result of the 1929 stock market crash was followed by a reform movement intended to assure an environment in which trust could be restored. Perhaps the greatest decline in trust since the 1929 crash has occurred within the past two decades.

Although there is evidence of an overall decline in client trust of professionals in the 1970s and 1980s, erosion of trust in stockbrokers was exacerbated by insider trading and junk bond scandals of the 1980s. These scandals led some people to doubt the fairness and integrity of the securities market, securities firms, and thus stockbrokers. The picture of greed and defiance of the law created by the scandals became identified not only with the Wall Street traders and arbitrageurs who were primarily involved, but with the securities industry in general (Tarabzadeh, et al. 1989:299).

ORGANIZATIONAL EMPLOYMENT OF PROFESSIONALS

Many scholars argue that organizational employment of professionals is likely to increase deprofessionalization (e.g. Carr-Saunders 1955; Wilensky 1964; Haug 1975, 1988; Derber 1983; Ritzer and Walczak 1988). However, there is little agreement on the attributes that are most vulnerable to bureaucratic pressures. Wilensky (1964) proposes that professionals in organizations may be more likely to lose sight of client needs and concludes that "perhaps

bureaucracy enfeebles the service ideal more than it threatens professional autonomy" (1964:148). However, Hall asserts that "Autonomy...is most strongly inversely related to bureaucratization" (1968:103).

Professional and bureaucratic principles of organization can be contradictory, but a number of scholars argue that we cannot assume these contradictions are present in organizational employment of professionals. Hall concludes that "an assumption of inherent conflict between the professional or the professional group and the employing organization appears to be unwarranted" (1968:104). Anleu (1992) found the connection between bureaucratization and deprofessionalization tenuous, and stated that there is "scant evidence that autonomy or monopoly over legal skills is jeopardized by employment in a bureaucratic organization" (1992:191). Freidson (1984) argues that, overall, "employment status is not a good, direct measure of control or lack of control over one's work" (1984:9).

In spite of these assurances of lack of inherent conflict in organizational employment of professionals, as organizationally based professional practices increased, research continued concerning the negative effects of organizational employment on professions. Much of this research in the 1980s and early 1990s (e.g. Freidson 1984; Rothman 1984; Ritzer and Walczak 1988; Scarpaci 1990; Anleu 1992) focused on external control of professions, which

contributes to deprofessionalization through limitation of autonomy (Ritzer and Walczak 1988:10).

This focus can be traced to political and economic factors in the 1980s. The United States had experienced a disruptive inflation-disinflation cycle between 1965 and 1980 (Segal 1989:147), and there was concern over the decline of America's international competitiveness (Segal 1989:114). In this uncertain economic climate, deregulation of several industries had far reaching economic consequences. In the trucking and airline industries deregulation led to vigorous price competition, route competition, and a series of mergers, all part of adjustment to a new competitive environment (Segal 1989:80).

The more competitive environment of the 1980s resulted in a period of unprecedented horizontal mergers, or expansion into closely related markets (Segal 1989:66). These mergers affected professionals because, as the size of organizations increased, there also tended to be an increase in managers from outside the profession with power over professionals (Gray 1986; Haug 1988; Ritzer and Walczak 1988).

Since autonomy and authority are generally seen as characteristics of professions, the "free" and independent professional has often been used as a bench mark to judge the effects of organizational employment. However Freidson (1984) argues that "this characteristic depiction of social

control within the professions has become too far removed from reality to be useful even as an ideal type" (1984:3).

Hall (1968) proposes that we can gain a better understanding of professionals by identifying differing types of organizational bases for professional occupations. The first type is the autonomous professional organization in which the professional has a great deal of control over his/her work and considerable input into organizational structure. A second type is the heteronomous professional organization in which professionals have less control over content of work than in autonomous professional organizations. Professionals in heteronomous professional organizations also have less control over organizational structure and policy. A third type of organizational setting is the professional department within a larger organization (1968:94).

Although autonomy is one of the characteristics used to identify professions, some professionals have always been in heteronomous professional organizations. Freidson (1984) notes that of the traditional professions, medicine, law, the clergy, the military, and university teaching, three of the five have never involved self employment (1984:9).

Hall (1968:95) places stockbrokers in the heteronomous category. Although they have individual clients and are compensated on a fee basis as are members of the autonomous group, their autonomy is limited by extensive rules of

various stock exchanges, the Securities and Exchange Commission as well as particular company policies.

Research on organizational employment of professionals has not led to the ability to predict effects of organizational employment on deprofessionalization. Rather, it has led to a realization of the complexity of the relationships involved. Professionals are in types of organizational structures that vary in degree of autonomy (Hall 1968:94). The conflict between bureaucratic norms and professional norms exists in varying degrees for different professions and for different groups within professions. There are no uniform patterns of deprofessionalization. At best, some regular trends appear from an overall treatment of professions. However, "for individual professions, the jurisdictional results of general social change depend on their particular situations" (Abbott 1988:150).

Strategic choice theory suggests that for professionals in organizations, organizational responses mediate the effects of environmental changes on deprofessionalization. Deprofessionalization has been affected not only by environmental changes, but also by diverse organizational responses to these changes. I do not consider strategic choice to be a substitute for the explanatory power of environmental changes on deprofessionalization, but I do consider it to be an important intervening variable that

contributes to an understanding of variation in deprofessionalization.

STATEMENT OF HYPOTHESIS

The environmental changes of jurisdictional competition, technological changes, and declining trust are not expected to affect professionals in all brokerage firms in a uniform way. It is expected, instead, that these environmental changes will be mediated by organizational responses, resulting in variation among firms in the deprofessionalization of stockbrokers.

CHAPTER 3

METHODOLOGY

The research questions of this study are:

First, in the period 1975-1990, how did brokerage firms differ in their response to bank deregulation?

Second, in the period 1975-1990, how did brokerage firms differ in their response to changes in technology?

Third, in the period 1975-1990, how did brokerage firms differ in their response to scandals within the industry?

Fourth, how did differences in organizational responses affect variation among firms in the deprofessionalization of stockbrokers?

I selected three brokerage firms as the basis of this study: Merrill Lynch & Company, Drexel Burnham & Company, and Charles Schwab & Company. I have used both quantitative and qualitative methods to answer the research questions. Quantitative content analysis is used to determine differences in organizational responses to environmental changes and qualitative analysis is used to examine variations in deprofessionalization resulting from differences in organizational responses within the three firms.

Numerous scholars identify jurisdictional competition, changes in technology, and declining client trust as environmental factors that affect deprofessionalization. Although environmental changes are generally considered to have a direct effect on deprofessionalization, strategic choice theory suggests that rather than these having a direct effect, outcomes at all levels of the organization are mediated by differences in organizational responses to various changes taking place outside the organization. In order to examine effects of differing organizational responses on the deprofessionalization of stockbrokers, I have used industry specific examples of environmental changes. These are: jurisdictional competition resulting from deregulation, changing technology within the securities industry, and scandals within the industry.

I consider these issues relevant for this project because they represent industry specific manifestations of environmental factors that are generally accepted as influences on deprofessionalization. Banking deregulation led to increased competition and a great deal of movement across previously protected boundaries. Therefore, I will use deregulation as an industry specific example of a change that is linked to jurisdictional competition. Scandals within the securities industry are examined as a specific area in which client distrust of stockbrokers intensified. Since changing technology is identified as a strong

influence in deprofessionalization, technological changes that affected the securities industry are also examined.

Response to environmental change within the profession of stockbroker takes place at various levels: individual stockbrokers, brokerage firms, National Association of Securities Dealers, Securities and Exchange Commission and stock exchanges. Responses from each of these levels could be examined, but in keeping with the theoretical basis of this study, firm-level responses to environmental changes will be examined. The unit of analysis, then, is the firm.

The time period of the study is January 1, 1975 through December 31, 1990, which was a period of extensive change within the brokerage industry. The May 1975 ruling of the Securities and Exchange Commission ended a period of almost two hundred years in which stock exchanges had fixed commission rates for all members. This ruling opened the door for discount brokerage services to be offered by banks and for the establishment of discount brokerage firms. Subsequent court rulings and decisions of the Federal Reserve Board continued to break down the wall between the jurisdictions of bankers and stockbrokers. Not only did bankers move into the jurisdiction of stockbrokers by offering discount brokerage services, but brokerage firms began offering accounts that included services such as checking and credit cards that were previously limited to banks. Deregulation brought confusion and competition into

areas in which there had previously been clearcut jurisdictional boundaries for bankers and stockbrokers.

Changing technology brought stock price information, reports from analysts, and client account information to stockbrokers more quickly than ever before. However, information was also more readily available to clients through various financial software programs, which had the potential of lessening clients' need for professional advice and expertise. Increased transaction speed and expanded information available through changing technology could benefit stockbrokers, but also had the potential of making these professionals little more than technicians.

During the time period studied there was an erosion of client trust toward professionals in general. For stockbrokers this decline in trust was exacerbated by extensive scandals within the securities industry during the 1980s.

COMPARATIVE APPROACH

I have used a comparative approach in this study, since comparative research has been used successfully to compare macrosocial units such as states, or cities, and has also been used for comparing groups or organizations (Quadagno and Knapp 1992). This type of research has been found useful for uncovering regularities in social processes which can then be subjected to further causal analysis (Abbott

1990). Comparative research seeks to explain similarities and differences in order to derive generalizations, challenge existing generalizations and assumptions, and clarify concepts. It is my intention in this study to use the comparative method to challenge the assumption that environmental changes have a direct effect on deprofessionalization.

One of the ways that comparative methodology differs from other types of analysis is that cases are purposefully selected, rather than using "homogeneous observations drawn haphazardly from a large pool of equally plausible selections" (Ragin 1991:1). Units are chosen because they are judged to be theoretically meaningful in ways that would invite comparison. I chose to compare Merrill Lynch & Company, Drexel Burnham & Company, and Charles Schwab & Company. These are three different types of firms, and each of them appears to have chosen different responses to the environmental changes of deregulation, changing technology, and scandals within the securities industry.

In this project, comparison of the three firms is used to ascertain whether or not the effects of environmental changes on deprofessionalization are mediated by organizational responses to these changes. This comparison follows the theoretical track established in the research questions. I examine differences in organizational responses to deregulation, changing technology, and

scandals, as well as ways in which differing responses resulted in deprofessionalization of stockbrokers.

Firms Chosen for Comparison

Merrill Lynch & Company Merrill Lynch traces its history to a partnership of Charles E. Merrill and Edmund C. Lynch begun in 1915. A number of sales and mergers through the years brought significant changes resulting in the firm of Merrill Lynch, E. A. Pierce & Cassett, which opened in 1940. This represents the beginning of the modern firm that Merrill envisioned as a "department store of finance" that would "bring Wall Street to Main Street" (Regan 1981:12). By the end of 1940 the firm had opened more than 12,000 new accounts for a total of 50,000, a total that grew to more than 2,000,000 by 1980 (Regan 1981:15). Merrill Lynch maintained a place among the largest companies in the industry throughout the period examined by this study (Porter 1983; Fortune June 4, 1990). Merrill Lynch emphasized innovation and quality in the development of a full service brokerage firm (Regan 1981). Innovative products were developed and new services introduced as the firm sought to offer a full range of financial services to its customers.

Drexel Burnham & Company Drexel Burnham & Company began in 1935 as Burnham & Company, a firm founded by I. W. Burnham. From 1935 to the early 1970s Burnham and Company was a small, undistinguished, but profitable brokerage house

(Bruck 1988). However, two seemingly unrelated events in the 1970s brought unprecedented change to Burnham & Company. In 1970 a twenty-three-year-old student at Wharton business school joined the Philadelphia-based investment firm of Drexel Firestone. His name was Michael Milken. In 1973 Burnham & Company merged with Drexel Firestone to create Drexel Burnham & Company, a move that resulted in the firm ranking fourteenth among brokerage firms in total capital by 1977 (Porter 1983). Drexel Firestone brought prestige and capital to Burnham & Company. Michael Milken brought success and notoriety to Drexel Burnham and triggered its eventual failure. In 1971 Burnham and Company had capital of $40 million (Bruck 1988:30); in 1985 the company's capital had increased to $1 billion, and Milken, Drexel's "junk bond king", reportedly earned $40 million (Business Week July 7, 1986:58).

By the mid 1970s Drexel Burnham was beginning to establish a specialized niche -- junk bonds (Stein 1992). Bond rating services consider these high-yield, high-risk bonds as speculations rather than investments. Consequently, this type bond had been virtually ignored by Wall Street. In 1977 Drexel Burnham raised money for three companies through sale of high-yield bonds and soon dominated the junk bond market, selling $100 billion worth of original-issue junk bonds by 1990 (Stone 1990:xiii).

Charles Schwab & Company   Charles Schwab & Company was incorporated in California in 1971, and was at that time a single-office conventional securities broker. In 1974 Schwab participated in a pilot discount commission program through the Securities and Exchange Commission, and after the 1975 ruling eliminating fixed commission rates, it began operating as a discount brokerage firm (Value Line Nov. 1990). By 1980 Charles Schwab was the largest discounter in the United States, with twenty branch offices and approximately 90,000 customers (Business Week Aug. 18, 1980:94). The firm continued its growth through the 1980s and by the beginning of 1990 it had grown to approximately 1.3 million accounts, 111 offices and 2,700 employees (Value Line Nov. 1990).

According to strategic choice theory, differences in organizational responses to environmental changes can be traced to numerous organizational factors, including size of the organization, financial resources, strength of competitive pressures on a particular firm, and the overall strengths and weaknesses of the company before the environmental changes occurred. Clearly the three companies analyzed in this study represent different kinds of firms which would be expected to respond differently to environmental changes. Specific differences in these organizations are elicited through content analysis, but the

choice of companies to be compared is based primarily on a general knowledge of differences in the firms.

DATA COLLECTION

Data for the study come from The Wall Street Journal and from three business periodicals. In the United States much of the information concerning economic and financial issues comes from The Wall Street Journal, which has been referred to as "the bible of financial/investment information newspapers" (Lesko 1988:27). Numerous business periodicals also offer concise, up-to-date information for those interested in financial topics. Therefore, I used content analysis to examine differences in organizational responses to the three environmental changes. Since the focus of the research is on jurisdictional competition as a result of deregulation, adoption of new technologies, and involvement in scandals, I have looked for mentions of these areas in the articles being analyzed.

Periodicals used for the study are Business Week, Fortune, and Institutional Investor. These periodicals were chosen for several reasons. In interviews with three veteran stockbrokers (Fowler 1993; Hodges 1993; Jackson 1993), Business Week and Fortune were suggested by all three brokers, and Institutional Investor was recommended by two of the three. Barron's and Forbes were also mentioned by two of the brokers, but both stated they would probably be

less useful for this study than other periodicals they had recommended. Barron's is a weekly newspaper for investors, with an emphasis on prices and analyses of stocks and bonds. Forbes focuses on features and profiles of financial executives and investment professionals (Lesko 1988). The Investor's Information Sourcebook (Lesko 1988) lists Business Week, Fortune, and Institutional Investor among the major investment and business-oriented periodicals published in the United States. Before making a final decision on choice of periodicals, I counted articles listed in the Index of Business Periodicals for 1990 for the three firms being compared. I found that approximately two-thirds of the articles with titles indicating relevance for this study were found in Business Week, Fortune, and Institutional Investor. Therefore, articles from Wall Street Journal, Business Week, Fortune, and Institutional Investor were examined for each of the companies in question.

The Wall Street Journal was founded in 1889 and is a leading daily financial/investment information newspaper with a 1990 circulation of 1,835,715 (Standard Rate and Data Service 1990). Business Week is an excellent source of general business news. This weekly magazine, founded in 1929, is published primarily for readers in management. Circulation in 1990 was 992,820 (Standard Rate and Data Service 1990). It offers a broad coverage of financial news, including sections on economic analysis and business

outlook (Lesko 1988:123). It often features news of investment firm activity that would be of interest to upper and mid-level business executives.

Fortune is published bimonthly by Time, Inc. It was established in 1930 and had a 1990 circulation of 781,040 (Standard Rate and Data Service 1990). Its audience is primarily middle and upper management. It gives information on economic, social, and political trends affecting the business environment (Lesko 1988). Institutional Investor is edited for financial and investment professionals. The magazine was established in 1967; it had a 1990 circulation of 136,394 (Standard Rate and Data Service 1990).

Two indexes were used to obtain articles to be examined: Wall Street Journal Index and Index of Business Periodicals. Information was examined for all articles indexed under the company names of Drexel Burnham & Company (or Drexel Burnham Lambert, Inc.), Merrill Lynch & Company (or Merrill Lynch, Pierce, Fenner & Smith, Inc.), and Charles Schwab & Company. The Wall Street Journal Index gives a short explanatory statement for each article. The Index of Business Periodicals usually gives titles only, but in some cases has a short explanation. For example, "Marriage Broker" includes "merger and acquisition department", and "Merrill Lynch's Asian Thriller" adds "Fung King Hey", which refers to the principal owner of Hong Kong's largest brokerage firm. In 1982 Merrill Lynch

acquired a percentage of Sun Hung Kai Securities and its affiliated bank.

Relevance of articles for use in the study was judged by the presence in the index listing of direct mention or inference concerning one or more of the categories in the coding design, found in Appendix A. For example, "Merrill Lynch Quacks Like a Bank", and "Firm's Bold Diversification into Bank-like Services was Bound to Rankle Bankers" are both clearly related to Merrill Lynch's movement into the area of banking services. "Firm expands from Stock to Gamut of Financial Services" is an indication of Merrill Lynch's use of full service as a competitive strategy. There is no doubt that "Drexel Sweats the SEC Probe" and "Drexel Agrees to Plead Guilty and Pay Out a Record $650 Million" refer to Drexel Burnham's involvement in scandals.

In some cases, recognition of a link to coding categories requires knowledge of the securities industry and the companies being compared. Without this knowledge the coder might overlook "The Firm That Fed on Wall Street's Scraps" as a reference to junk bonds, or miss "Has Merrill Found a Way to Soothe Baldwin Customers?" as a reference to efforts to solve problems associated with a major scandal involving Merrill Lynch. Knowing that Drexel Burnham's annual High Yield Bond Conference was referred to as the "Predator's Ball" clarifies the statement, "And Now, the Predator is Preyed Upon".

However, information on some articles was ambiguous. Titles such as "Merrill Lynch's Not-So-Thundering Recovery Plan", "Power on Wall Street", and "The Junk Market's Black Hole" do not give a clear indication of a link to the categories used in the content analysis. Articles with titles indicating a connection to the issues of the study, and those with ambiguous information were scanned. Of this group, 412 articles were judged to contain information relevant to this study. I used these articles for the content analysis.

QUANTITATIVE ANALYSIS

I have used content analysis to determine variation in organizational responses to deregulation, changing technology, and scandals, which were key environmental changes in the brokerage industry during the period 1975 through 1990. There are many possible schemes for classifying content data. For this study I developed indicators to reflect the purposes of the project, as seen in the research questions.

The content analysis uses the selected group of 412 articles to identify differences in Drexel Burnham, Merrill Lynch, and Charles Schwab in terms of their organizational responses to industry specific environmental changes. The descriptive statistics of the content analysis provide a starting point for the second phase of the project, which is

the examination of effects of organizational responses on variation in deprofessionalization among professionals in the organizations.

The coding design, (Appendix A), was used to categorize the content of the articles being analyzed. I have coded articles by periodicals in which they appeared, by month and year, and by firm referred to in the article. Other categories in the coding design are organized around the first three research questions.

The first group of categories has to do with jurisdictional competition. This includes movement of bankers into the jurisdiction of stockbrokers as well as movement of brokerage firms into new areas. Three new areas for brokerage firms are coded: banking services, insurance products, and real estate. Deprofessionalization theory considers jurisdictional competition as an important aspect of maintaining, gaining, or losing power as a profession. Therefore, it is crucial to identify these movements into new areas, in this case representing organizational rather than professional decisions.

Another aspect of jurisdictional competition in response to deregulation involves competitive strategies chosen by the companies being analyzed. It is expected that variation in choice of competitive strategies will lead not only to differing outcomes for the firms, but also will lead to variation in deprofessionalization of stockbrokers.

Several competitive strategies are enumerated by strategic choice theory. For this project four strategies are identified in the content analysis: low cost, full service, special niche, and mergers and acquisitions.

The second group of categories concerns organizational responses to changes in technology. Mentions of adoption of new technology are noted in three areas: information services, which brings more information in less time to stockbroker and clients; program trading, which allows more efficient trading of groups of stocks; and market services, which involves new or more efficient ways of placing orders or trading stocks and bonds (other than program trading).

The third group of categories delineates organizational involvement in scandals within the securities industry. Six types of scandals are identified. In addition to type of scandals, mentions of company involvement in solutions are coded. Articles are included in this category if they provide a solution that will be helpful to clients, or if the company distances itself from the person or persons causing the problem. Primarily these articles mention full or partial reimbursement of losses incurred by clients. Company solutions to problems involved in scandals are likely to be helpful to the firm's reputation and, in turn, increase client trust in stockbrokers employed by that organization.

QUALITATIVE ANALYSIS

By combining quantitative and qualitative methodology I am able to build on the strengths of both approaches. Holsti suggests that "the content analyst should use qualitative and quantitative methods to supplement each other. It is by moving back and forth between these approaches that the investigator is most likely to gain insight into the meaning of his data" (1969:11). I have included qualitative methodology because it is particularly useful for those research questions in which relevant interconnections have not been clearly identified (Marshall 1985). Qualitative research bases interpretation of causal relationships on observable concrete interconnections as they exist within a particular setting. Qualitative interpretation of the complex issues of environmental changes and organizational responses is expected to enhance understanding of the variation among firms in deprofessionalization of stockbrokers during the period of 1975 to 1990. Qualitative analysis also places a strong emphasis on change over time, and on explanation within context, which makes it particularly useful to this study.

I have used the results of the content analysis, along with concepts of deprofessionalization and strategic choice theory to answer the fourth research question: How did these organizational responses affect the professionals within the firms in terms of deprofessionalization? Since

the articles analyzed in this study are business news articles, there are no direct references to deprofessionalization. Consequently the presence or absence of deprofessionalization will have to be inferred, much like Durkheim infers the presence or absence of group integration when studying suicide. In this study then, the concept of deprofessionalization is measured by indications in the articles of decreases in two widely recognized characteristics of professionals: autonomy and client trust. Loss of autonomy is indicated by apparent changes in control and content of work. Decrease in client trust is indicated by the extent of firm involvement in scandals.

The qualitative portion of the project is guided by several questions:

1 - What effects, if any, did organizational responses have on control of work?

2 - What effects, if any, did organizational responses have on content of work?

3 - What effects, if any, did involvement in scandals have on company reputation?

4 - What effects, if any, did company solutions to problems related to scandals have on company reputation?

5 - Did some organizational responses have a stronger effect on deprofessionalization than others?

I chose these questions because they address probable links of organizational response and deprofessionalization.

Control of work and content of work are both related to autonomy, which is recognized as one of the identifying characteristics of professionals. Abbott (1988) emphasizes the centrality of control of work and content of work in understanding deprofessionalization. Literature on trust suggests that trustworthiness of professionals within an organization is tied to the perceived trustworthiness of the organization. Since it is unlikely that the effects of all organizational responses are similar, the final question focuses on differences in effects of organizational responses on deprofessionalization.

RELIABILITY AND VALIDITY

No coders other than the researcher were used in the study. In content analysis research it is common to have a single researcher as the exclusive coder of content when project size permits. Content analysis frequently relies on content validity, which "is usually established by the informed judgment of the investigator" (Holsti 1969:143). Berelson (1952) indicates that validity is seldom a major problem in content analysis since the issue of validity can usually be dealt with by "careful definition of categories and judicious selection of indicators" (Berelson 1952:171).

Reliability problems in content analysis are usually the result of ambiguity of word meanings or category definitions. In content analysis, reliability is a function

of the coder's insight and skill, clarity of categories, and degree of ambiguity (or lack thereof) in the data (Holsti 1969). These criteria of content analysis reliability are met in this project by my knowledge of the brokerage industry, gained by working as a registered sales assistant in a brokerage firm, the straightforward nature of the articles being analyzed, and the care taken in establishing clearcut categories for analysis.

Although I did not have another coder with similar familiarity and knowledge of the securities industry, a colleague agreed to code several articles. She also reviewed the exhaustiveness and mutual exclusivity of the schema I developed to categorize the articles analyzed for this study. In each instance my colleague, acting as an independent judge, reached conclusions which were identical to mine.

SUMMARY

Using a comparative approach, three brokerage firms were selected to study because they are expected to have differing responses to the environmental changes of jurisdictional competition, technological changes, and declining client trust. Both quantitative and qualitative analysis are used in the project.

Quantitative content analysis of a selected group of 412 articles provides descriptive statistics concerning

differences in organizational responses. Qualitative analysis examines the relationship between differing organizational responses and variation in deprofessionalization.

CHAPTER 4

QUANTITATIVE ANALYSIS

This chapter presents the statistical analysis of variation in organizational responses of Drexel Burnham, Merrill Lynch, and Charles Schwab to three environmental changes: jurisdictional competition resulting from deregulation, changing technology, and widespread scandals. This analysis is primarily descriptive in nature.

In order to examine the possible effects of organizational responses on variation in deprofessionalization of stockbrokers, the differences in responses among the firms must first be identified. The quantitative content analysis, which is the first phase of the project, identifies these differences and provides a foundation for further analysis concerning the relationship of differences in organizational responses and variation in deprofessionalization. Four hundred twenty-four observations, henceforth called "cases", are drawn from the 412 articles selected for analysis. Table 4.1 shows frequency of cases by year and by firm.

TABLE 4.1

ARTICLES FOR YEARS 1975 - 1990
FREQUENCIES AND PERCENTAGES: BY FIRM

Year Published	Drexel Burnham n (%)	Merrill Lynch n (%)	Charles Schwab n (%)
1975	-0	2 (1)	-0-
1976	-0-	-0-	-0-
1977	-0-	-0-	-0-
1978	-0-	2 (1)	-0-
1979	-0-	1 (1)	-0-
1980	-0-	5 (4)	2 (5)
1981	1 (1)	2 (1)	2 (5)
1982	-0-	9 (6)	2 (5)
1983	-0-	17 (12)	4 (9)
1984	11 (5)	34 (24)	5 (11)
1985	5 (2)	17 (12)	3 (7)
1986	33 (14)	15 (10)	6 (13)
1987	29 (12)	16 (11)	8 (18)
1988	67 (28)	7 (5)	7 (16)
1989	71 (30)	12 (8)	4 (9)
1990	18 (8)	6 (4)	1 (2)
TOTALS	235 (100)	145 (100)	44 (100)

Sources: <u>Wall Street Journal</u>, <u>Business Week</u>, <u>Fortune</u>, <u>Institutional Investor</u>

Drexel Burnham was virtually ignored by the business press concerning topics of this study for the years 1975 through 1983, with only one of the 235 Drexel Burnham cases appearing in this time period. Although articles pertaining to Drexel Burnham account for 55 percent of the total 424 cases, 234 of these appeared after 1983. Merrill Lynch and Charles Schwab also show higher frequencies during the 1984 - 1990 period, but with fewer dramatic differences than those shown by Drexel Burnham. The latter seven years show 107 mentions of Merrill Lynch, which is 74 percent of the Merrill Lynch cases, and 34 mentions of Charles Schwab which accounts for 77 percent of the 44 Schwab cases.

There are a number of possible explanations for the paucity of cases in the early years of the study. The 1975 ruling ending fixed commission rates was chosen as an appropriate time for beginning the content analysis because it activated a series of changes in the financial marketplace. Although hindsight gives a good view of this process of change, it may not have been as evident at that time. Court rulings and Federal Reserve Board decisions in the early 1980s continued to break down the regulatory wall separating banks and brokerage firms. Changes were, for the most part, gradual and for this reason may have attracted little press attention in the first few years after the beginning of the deregulation process.

The clustering of virtually all Drexel Burnham cases in the last seven years of the study requires further explanation. Although the 1973 merger with Drexel Firestone brought capital and Michael Milken into the new firm of Drexel Burnham & Company, the company remained rather undistinguished for several years. During these years Milken was promoting his ideas about the profitability of junk bonds and building a place for himself as the "junk bond king".

A 1990 article notes that "as early as 1984, Drexel was trying to monopolize the high-yield business". (Fortune May 21, 1990:90). It is also in 1984, as Table 4.1 shows, that we note an increase in articles about Drexel Burnham, with 11 cases in 1984 compared to only one mention for the previous nine years. The next increase occurs in 1986 when there are 33 mentions of Drexel Burnham. This was a year in which Dennis Levine, a Drexel investment banker, was charged with insider trading and Ivan Boesky, a longtime Milken client, pleaded guilty to SEC charges of insider-trading violations. After that time Drexel Burnham became increasingly entangled in scandals and increasingly newsworthy; in 1988 there are 67 mentions of Drexel Burnham and 71 mentions in 1989.

JURISDICTIONAL COMPETITION
ASSOCIATED WITH BANK DEREGULATION

Competitive shocks, such as bank deregulation, often result in an increased likelihood of jurisdictional borders being crossed by other professions. In answering the question of how brokerage firms responded to bank deregulation, my coding design uses three categories dealing with jurisdictional competition. The first issue I examine is movement of bankers into areas previously limited to stockbrokers, next the movement of stockbrokers into areas previously occupied by bankers and other professionals and finally the competitive strategies used by brokerage firms.

Movement of Bankers into Areas Previously Limited to Stockbrokers

Only 12 cases (3%) mention bankers moving into the jurisdiction of stockbrokers. Primarily, articles in this category deal with the BankAmerica purchase of Charles Schwab & Company. This was a widely publicized acquisition, since it linked the nation's largest bank holding company with the leading discount brokerage firm. Also, the move, made in 1982, predated much of the bank movement into stock brokerage. BankAmerica considered this purchase would "get the jump on the banking industry in moving into a lucrative new business" (Business Week Aug. 2, 1982:20). In approving this case the Federal Reserve Board for the first time ruled that discount brokerage services were "closely related to

banking" (Wall Street Journal June 18, 1984:25). Because Schwab was not involved in underwriting corporate securities, BankAmerica "believed it had found a way around federal regulations that have long kept banks out of the securities trade"(Business Week Aug. 2, 1982:20).

Although banks and brokers were said to be "constantly at war, each accusing the other of stepping on the opponent's turf" (Wall Street Journal Feb. 15, 1984:33), banks also formed some business ties with brokerage firms. For example, Bank One in Columbus, Ohio, provided data processing for the credit card and checking operations of Merrill Lynch & Company. Advocates of these ties argued that "selling their services to brokers and others is a good strategy in the face of deregulation in the financial services industry. They say that it allows banks to expand their product line, earn extra fees and perhaps develop a niche in the financial world as data processors" (Wall Street Journal Feb. 15, 1984:33).

The impact of bankers moving into jurisdictions of stockbrokers is undoubtedly underestimated by the three percent of articles mentioning this movement. Since I selected articles because of the mention of specific brokerage firms, encroachment of bankers would be noted only if directly related to one of the three brokerage firms being analyzed. Because of this limitation, this aspect of jurisdictional competition between stockbrokers and bankers

cannot be accurately assessed within the scope of this analysis. However, other sources (e.g. Coler 1989; Khoury 1990) indicate that the encroachment evident in the cases concerning BankAmerica is only one example of widespread jurisdictional competition between bankers and stockbrokers.

Movement of Brokerage Firms into Jurisdictions of Other Professions

I examine brokerage firm movement into three new areas: banking services, insurance products, and real estate. Table 4.2 shows Charles Schwab and Merrill Lynch making some movement into new areas, but there are no mentions of Drexel Burnham moving into any of these three areas. For Charles Schwab there are five mentions (11%) of movement into banking services, two mentions (5%) of insurance products, and one mention (2%) of movement into real estate. Merrill Lynch exhibits the most movement into new areas with ten mentions (7%) of Merrill Lynch's movement into insurance products, and eleven mentions (8%) of real estate, and twenty five mentions (17%) of movement into banking services. Titles such as "Merrill Lynch Quacks Like a Bank", "Merrill Lynch's Latest Bombshell for Bankers", and "Merrill Lynch Plays Bank -- Again" suggest Merrill Lynch's continuing presence in banking services.

Banking Services Merrill Lynch's encroachment on banking turf began with its introduction of Ready Assets Trust, a money market fund, in 1975. A combination of

TABLE 4.2

TABLE 4.2

STOCKBROKER MOVEMENT INTO NEW AREAS
FREQUENCIES AND PERCENTAGES: BY FIRM
1975 - 1990

New Areas	Drexel Burnham n (%)		Merrill Lynch n (%)		Charles Schwab n (%)	
Banking Services	-0-		25	(17)	5	(11)
Insurance Products	-0-		10	(7)	2	(5)
Real Estate	-0-		11	(8)	1	(2)
No Mention	235	(100)	99	(68)	36	(82)
TOTALS	235	(100)	145	(100)	44	(100)

Sources: Wall Street Journal
Business Week
Fortune
Institutional Investor

financial circumstances created the possibility of success for money market funds offered by large brokerage houses. Banks were subject to Federal Reserve regulation of interest rate ceilings, but nondepository institutions were not included. This gave brokerage firms a distinct advantage during a period in which the market interest rate was considerably higher than bank interest rate ceilings. Ready Assets Trust, valued at $11.4 billion in 1980, became one of the largest and most popular money market funds (Wall Street Journal Sept. 10, 1980:18).

Merrill Lynch's introduction of its Cash Management Account in 1977 was considered "even more threatening to banks" than Ready Assets Trust (Wall Street Journal Sept. 10, 1980:18). The Cash Management Account was described by Merrill Lynch as the "first truly modern brokerage account" (Institutional Investor Sept. 1981:37) and by others as the "latest development in banker-broker jockeying", which had the banking community "rumbling with reaction" as many bankers objected to Merrill Lynch being on their turf (Wall Street Journal June 22, 1977:2). Although bankers insisted that Merrill Lynch be subjected to "the same regulations and restrictions as commercial banks", the Federal Reserve Board stated that Merrill Lynch's plan did not violate the Glass-Steagall Act which separates commercial and investment banks (Wall Street Journal July 20, 1977:4). The Cash Management Account was later copied by banks and by other brokerage

firms "although much less successfully". Five years after its introduction Merrill Lynch still dominated the field with almost 900,000 of the estimated 1.1 million accounts of this type (Wall Street Journal Nov. 15, 1982:31), and in 1984 Merrill Lynch still had nearly ten times the Cash Management Accounts of its nearest rival (Wall Street Journal March 12, 1984:18).

The Cash Management Account has features similar to bank savings and checking accounts. It offers a high-yield money market fund, check-writing privileges, access to brokerage services, and a credit card or debit card for cash withdrawals. Any dividends, interest, or proceeds of securities sales are automatically swept weekly into the money market fund, with the option of having amounts over $1,000 swept immediately (Fortune Oct. 20, 1980:135). The Cash Management Account also includes a line of credit, usually a standard Wall Street margin account, in which the brokerage firm lends clients up to 50 percent of the purchase price of the securities being held in their account (Securities Industry Association 1992:212).

This new type of brokerage account offered advantages of both bank and securities accounts. Clients had quick and easy access to funds through checks and credit card. One of the developers of the CMA said, "We've made our customers' investments more valuable by taking them to the ultimate of liquidity" (Fortune Oct. 10, 1980:135). Any idle funds were

swept into the high interest money-market, and loans were available through the credit line. The interest rate charged on loans for nonsecurities purposes was the same as for securities purchases; this rate was substantially less than charged by bank-card operations.

In 1984 Merrill Lynch expanded the services of this account even further through an agreement with Safeway Stores which enabled its CMA customers to use cash dispensing machines located in Safeway supermarkets. This move was depicted as "the latest competitive blow struck by national brokerage firms at the banking industry" (Wall Street Journal Jan. 13, 1984:35). As automatic teller machines became more widespread, other firms were able to offer similar services, but Merrill Lynch once again proved itself to be a leader among brokerage firms in offering banking services.

Merrill Lynch's Cash Management Account is described as "a revolutionary selling tool for brokerage services" (Fortune Oct. 20, 1980:135) and as "a glitteringly creative idea that...offers benefits no bank can match" (Fortune April 19,1982:67). A 1980 article notes that the Cash Management Account "may be the most important financial innovation in years. It is widely viewed as the intrusion of a brokerage house into the turf formerly reserved for banks" (Fortune Oct. 20, 1980:135).

The significance of this type of account seemed to grow rather than diminish over time. In 1982 cash management accounts were considered "a major factor in the competition for personal assets being waged by banks, brokers and... financial conglomerates" (Wall Street Journal Nov. 15, 1982:31). A 1984 article notes that brokerage firm officials consider this type account to be "required to retain control of customers' assets as deregulation spreads through the industry" (Wall Street Journal March 12, 1984:18). Between 1977 and 1986 Cash Management Accounts brought Merrill Lynch more than $125 billion in deposits (Fortune July 21, 1986:10).

Because of the popularity of the Cash Management Account, Merrill Lynch developed several variations on the theme. In 1982 the firm designed an international CMA and offered it in a number of countries including Britain, Kuwait, Bahrain and Dhabi (Wall Street Journal Nov. 15, 1982:31). The Capital Builder Account was introduced in 1984. This account, referred to as "Son of CMA" by industry insiders, was a streamlined and lower priced version of the CMA. The annual fee was about $20 and it required a minimum investment of only $5,000, compared to the $50 fee and minimum investment of $20,000 for the Cash Management Account. Also, unlike the CMA, the Capital Builder Account did not have unlimited use of services. For example, check writing privileges were included, but customers were

required to pay for each check written above a designated monthly limit. Merrill Lynch claimed that the average CMA customer was likely to maintain his/her banking connections and use the CMA as an additional account. However, the Capital Builder Account was more likely to attract the kind of customer who would use this instead of his/her present bank account (Wall Street Journal March 12, 1984:18).

In 1986 Merrill Lynch introduced the Working Capital Management Account, "tailored to small and medium-size businesses, a market hitherto dominated by regional and community banks" (Fortune July 21, 1986:10). With the introduction of this account small banks faced the possibility of losing valuable corporate clients. Like the CMA, the WCMA pulled together a number of financial services into one account. There was a line of credit that could range from $200 to $400 million, a variety of insurance and pension services, and no-load money market funds. The WCMA customer could also move money to or from other bank accounts and write paychecks (Fortune July 21, 1986:10; Institutional Investor Jan. 1986:260).

Merrill Lynch was not only the most heavily involved of the three firms in movement into banking services, but also exhibited this movement in a variety of ways. Although the Cash Management Account was the firm's major coup in terms of banking services, it certainly was not the only way in

which the encroachment into bankers' jurisdiction took place.

In 1982 Merrill Lynch enlarged its presence in banking services by beginning to sell certificates of deposit. The company was "quietly springing yet another surprise on the banking industry...Bankers...see it as another threat to their customer and core deposit bases" (Business Week June 28, 1982:92). However, Merrill Lynch managed to elude bank regulations because it was not "accepting" consumer time deposits, but was transferring these funds to a bank which paid Merrill Lynch a commission. Also, because Merrill Lynch was not technically the issuer of the CDs, it could buy them back from customers without early withdrawal penalties. This expansion of banking services angered bankers. One bank official said, "Merrill Lynch is getting to the point where it can tell people they don't need to go to a bank anymore, and that concerns us" (Business Week June 28, 1982:92).

In 1983 Merrill Lynch brought another challenge to banks:

> Merrill Lynch & Co. is moving into banks' turf again--this time seeking to fill a foreign exchange niche that U. S. commercial banks have largely ignored...It's bringing big time foreign exchange to mainstream America in its latest challenge to the banks (Business Week Nov. 14, 1983:71).

Banks discouraged smaller foreign exchange deals by charging higher premiums for transactions of less that $1 million.

While their fees for these smaller transactions could run as high as 2 percent of the total amount, Merrill Lynch was willing to negotiate commissions which resulted in maximum charges of .25 percent of the transaction.

Merrill Lynch not only found ways to offer many banking services, but also made a direct entry into the banking business when the New Jersey banking commissioner gave the firm approval to form a state bank in New Jersey. In order to circumvent banking regulations, the bank did not accept demand deposits or checking accounts, but did make commercial loans, accept time deposits and offer trust-related services. This move was seen as "yet another indication that the traditional barriers separating banking and securities industries are breaking down" (Wall Street Journal Jan. 4, 1984:4).

Although Charles Schwab was not as extensively involved in banking services as Merrill Lynch, it did make some moves into the area of banking services. For example, Schwab was one of several brokerage firms to enter into agreements in 1981 with Bank One of Columbus, Ohio, for check processing and with Visa USA for credit card processing. These agreements made it possible for Schwab to offer a cash management account (Wall Street Journal June 26, 1981:10). By 1990 Charles Schwab was holding "$2.9 billion of client cash in its highly successful Schwab One cash management accounts" (Business Week March 19, 1990:102). The firm also

sells certificates of deposit and offers money market accounts and retirement accounts.

Insurance Products Two articles mention Charles Schwab's involvement in insurance products. A 1981 article states that Schwab had developed an insurance brokerage unit that would "provide customers with comparative costs of life insurance policies" but makes no mention of other services that might be offered by the unit (Wall Street Journal Aug. 5, 1981:21). The other mention is a statement indicating at the time Charles Schwab & Company went public in 1987 there were plans to offer "new investment products, including. . . insurance" (Wall Street Journal Aug. 3, 1987:4).

The ten mentions of Merrill Lynch's entry into the area of insurance products indicate extensive involvement in this area. Annuities were among the first insurance products offered by brokerage firms, since they offer a natural link with brokerage services related to retirement planning. An annuity generally guarantees a lifetime income at retirement or at a specified age. The type annuities usually sold by brokerage firms are called single premium deferred annuities. Buyers make a single payment and taxes on the interest is deferred until the money is withdrawn, usually after retirement (Wall Street Journal April 18, 1983:18).

However, insurance products sold by Merrill Lynch were not limited to annuities. The company was one of three brokerage firms to "link up with insurers to repackage some

standard insurance policies as tax-favored retirement savings plans" (Wall Street Journal Feb. 2, 1989:C1). These policies, called universal life insurance, combine a death benefit along with tax-favored savings. "In effect, part of each premium dollar goes to pay for the death benefit and expenses; the rest earns interest at a rate set periodically by the insurer" (Wall Street Journal Feb. 2, 1989:C1).

Merrill Lynch's interest in insurance sales led the company to institute a program of in-house insurance specialists, with no clients of their own, who worked with the stockbrokers. The insurance program, which in 1986 included 110 specialists, was credited with boosting annual revenues from insurance from $90 million in 1980 to $171 million in 1984 (Institutional Investor Jan. 1986:258).

Real Estate The only mention of Charles Schwab in connection with real estate is the inclusion of real estate in the list of new products to be offered by the firm after it became a publicly owned company in 1987. However, Merrill Lynch made its presence felt in the real estate market. A 1979 article states:

> Beginning some time soon, a growing number of Americans will find that Merrill Lynch & Co. has become their broker, their real-estate broker, that is. The bulls are being sent out to graze on the lush lawns of the residential brokerage business, and real estate brokers around the country agree that the invasion is a major event for their industry (Fortune Jan. 29, 1979:86).

In 1979 the real estate industry was changing from a primarily localized business to one that was expected to be dominated by regional and national companies within five years. Merrill Lynch was the "biggest to jump in yet, and its entry suggests what had been a solution is turning into a revolution" (Fortune Jan. 29, 1979:86). Merrill Lynch said it would not cut commissions, but would offer "more service for the same fee". However, there was no doubt that its entrance into the field would provide formidable competition not only for marginal firms, but for solid larger firms as well. The owner of a Houston realty firm with six offices and fifty employees said, "there's no question we'll have trouble with the giants like Merrill" (Fortune Jan. 29, 1979:88). Merrill Lynch predicted that by the mid-1980s it would be a "top contender in the 50 most lucrative real estate markets in the U.S." (Wall Street Journal Sept. 10, 1980:5).

A 1985 article states that Merrill Lynch "now has more people selling real estate than corporate securities. That's perhaps the most striking measure of how far Merrill Lynch has plunged into the real estate business" (Wall Street Journal April 3, 1985:33). However its profits from real estate were portrayed as "paltry". Merrill Lynch entered the real estate business at the peak of the housing market in 1979 which was followed by a prolonged housing recession. Although the drop in housing starts forced the

firm to cut back on some of its real estate plans, it remained optimistic that the real estate operations would "turn the corner" by 1983 (Institutional Investor Sept. 1981:45).

In 1985 Merrill Lynch was said to show "no signs of backing away from real estate", but in September of 1986 it announced that its real estate businesses were for sale. The sale was portrayed as a "recognition that real estate customers won't necessarily become securities investors--and vice-versa" (Wall Street Journal Sept. 30, 1986:3). The company said it would put the proceeds of the real estate sale, estimated at $500 to $800 million, into expansion overseas, new consumer insurance products and investments in back-office technology, which were considered more profitable alternatives (Business Week Oct. 13, 1986; Fortune Oct. 27, 1986).

Competitive Strategies

Competitive strategies make up the third category dealing with jurisdictional competition. Four competitive strategies are examined: (1) low cost, (2) full service, (3) special niche, and (4) mergers and acquisitions. Table 4.3 identifies different patterns of competitive strategies for each of the three companies being compared.

As indicated in Table 4.3, Drexel Burnham & Company depends almost exclusively on the strategy of establishing a

TABLE 4.3

COMPETITIVE STRATEGIES
FREQUENCIES AND PERCENTAGES: BY FIRM
1975 - 1990

Competitive Strategies	Drexel Burnham n (%)	Merrill Lynch n (%)	Charles Schwab n (%)
Low Cost	-0-	2 (1)	18 (41)
Full Service	-0-	28 (19)	5 (11)
Special Niche	64 (27)	-0-	-0-
Mergers and Acquisitions	2 (1)	14 (10)	4 (9)
No Mention	169 (72)	101 (70)	17 (39)
TOTALS	235 (100)	145 (100)	44 (100)

Sources: *Wall Street Journal*
Business Week
Fortune
Institutional Investor

special market. The special niche strategy accounts for 27 percent (64 cases) of all Drexel Burnham cases. The only other mentions of competitive strategies for this firm are two mentions (1%) of mergers and acquisitions.

As expected, the primary strategy for discounter Charles Schwab & Company was low cost. There were 18 mentions (41%) of this strategy for Schwab. However, there were also five mentions (11%) of full service and four mentions (9%) of mergers and acquisitions.

Merrill Lynch & Company has 28 references (19%) to full service, 14 mentions (10%) of mergers and acquisitions, and two cases (1%) of low cost. Although Merrill Lynch is not as sharply focused on one strategy as the other two firms, it clearly favors providing full service as its leading competitive strategy.

Low Cost The 1975 ruling ending fixed commission rates opened the possibility of cost-reduction as a competitive strategy for brokerage firms. The hallmarks of this strategy include lowering wages and minimizing overhead. Discount brokers could lower wages by utilizing salaried employees instead of commissioned stockbrokers and could minimize overhead by reducing services. In fact, these changes constitute defining characteristics of discount brokers. "Discounters do not employ commissioned salespeople, nor do they dispense investment advice or research. They simply take orders to buy and sell

securities" (Business Week May 1986:80). Discount brokers can achieve cost reduction by employing licensed brokers as salaried employees.

Charles Schwab leads the three firms in the use of low cost as a competitive strategy. Eighteen of the twenty cases concerning low cost pertain to this discount brokerage firm. No mentions are made of Drexel Burnham in connection with low cost strategies, but two articles about Merrill Lynch indicate that other firms are not completely without concern for cost cutting as a competitive strategy.

One example of Merrill Lynch's use of a low cost strategy is the "unbundling" of individual commissions. "That is, the services traditionally covered by the commissions--execution of orders, research, custodial services, etc.--are being charged for separately. The customer can buy as much or as little as he wants" (Fortune May 1975:153)

Another example of Merrill's use of low cost as a competitive strategy is the Blueprint program. Employees of companies participating in the program could make trades in their retirement plans and stock-ownership plans at discounts up to 55 percent. It was expected that this plan, "aimed at the savings dollar of the American public", could "pose a competitive challenge for discount brokers, mutual funds, and banks" (Business Week March 30, 1987:72).

Full Service Another widely used competitive strategy in the securities industry involves striving to be a full service brokerage firm, which emphasizes attracting and maintaining clients through diversity of services offered. Of the 33 cases mentioning full service as a competitive strategy, 28 (85%) pertained to Merrill Lynch, and the other five (15%) mention Charles Schwab.

Although the increased competition of the period being studied may have intensified Merrill Lynch's emphasis on full service, "creating new products and services has always been a Merrill Lynch strength" (Business Week July 9, 1984:90). In a 1981 article Merrill Lynch is said to have been "grudgingly regarded by competitors as perhaps the most innovative and far-thinking firm on Wall Street" (Institutional Investor Sept. 1981:37).

This full service strategy is characterized in a variety of ways by those inside and outside the firm. Merrill Lynch is considered to offer a wider variety of products to its customers than its competitors. It is seen as an "innovative multi-faceted financial services company instead of just a seller of stocks and bonds" (Business Week June 18, 1984:31). The hope of Merrill Lynch was to have brokers who would "enter into every one of their clients' financial decisions from the time they begin earning income to the day they retire" (Institutional Investor Jan. 1986:257). This idea is expressed in a stronger, but perhaps

less flattering way, when it is said that Merrill Lynch had a "grand plan to offer womb-to-tomb financial services to just about everyone with a nickel in his pocket" (Fortune Aug. 6 1984:77). A company spokesman said, "We don't want to leave any cracks in the dike where clients would be inclined to go do business with somebody else" (Institutional Investor Jan. 1986:258). Merrill Lynch Chairman Donald Regan declared: "What we're trying to do is to see how many financial services we can perform for people--legally and profitably" (Wall Street Journal Sept. 10, 1980:5).

As Merrill Lynch continued to be a leader in areas such as banking services, its reputation as a full service brokerage firm was enhanced. "Many banks have business arrangements with local securities brokers, but cannot compete with Merrill Lynch's range of services" (Fortune July 21, 1986:10). A bank trader commented: "Merrill Lynch's move into foreign exchange not only moved them into bankers' jurisdiction, but was another way of exhibiting their commitment of full service to their customers" (Business Week Nov. 14, 1983:71).

Although low cost was the primary strategy used by Charles Schwab, the firm also sought to "diversify its product line" and differentiate itself from the typical discount broker by offering "more than the bare-bones services of most discounters" (Business Week May 12,

1986:81). Schwab offered a broad mix of products and services including a cash management account, certificates of deposit, retirement accounts, and mutual funds (Business Week May 19, 1990:102).

Special Niche One of the primary competitive strategies involves seeking out a specialized market niche. Drexel Burnham chose this strategy as evidenced by frequent mention of the firm as a "dominant force in junk bonds", a "junk-bond juggernaut", "ruler of the high-yield kingdom", and "undisputed champion of junk bonds". It was said that Drexel "clamped a hammerlock on the market for high-yield, high risk bonds" and had "muscle and mystique that made it the Mike Tyson of the junk bond market". None of the articles mention Merrill Lynch or Charles Schwab in connection with choosing a special market niche. However, of the 66 cases mentioning Drexel's use of competitive strategies, 64 cases (97%) had to do with choosing a special market niche; the special niche for Drexel was trading junk bonds.

Drexel Burnham brought junk bonds to the attention of Americans, but these high risk debt securities were not new to the financial marketplace. Bond issues are evaluated by several rating services and these ratings are published. Bond ratings are based on the issuer's creditworthiness or projected ability to make timely interest and principal payments. Federal and state banking authorities have

established policies determining which securities banks can purchase. These higher rated bonds are referred to as bank grade or investment grade bonds. Bonds with lower ratings are considered to be speculative or non-investment grade bonds (Securities Industry Association 1992:25). The securities industry prefers to call these bonds high-yield bonds because of interest that is typically two to three percentage points higher than investment grade bonds. However, in spite of the higher yield, the bonds are difficult to sell because of the risk associated with them. It is these higher-risk bonds that provided Drexel Burnham with the special niche that made it both famous and infamous. It is these speculative debt securities that came to be known as junk bonds, although Drexel Burnham tried without success to change the terminology to "fallen angels".

During the mid-1970s there was a definite "hole" in the bond underwriting business for speculative bonds. Junk bonds were considered a "sleepy little corner" of the debt securities market, but Drexel turned them into "one of the hottest and most controversial of financial instruments". The firm was a "second-rate investment house until it went after business its status-conscious rivals found demeaning--trading junk bonds and financing obscure and struggling companies" (<u>Fortune</u> Sept. 3, 1984:89). "Excluded from the clubby Wall Street power structure, Drexel...built from

scratch a vast new power base of its own" (Business Week July 7, 1986:57).

As early as 1981 the business press noted that Drexel had "carved out an impressive niche for itself...While its rivals tried to be all things to all companies, Drexel Burnham Lambert took aim at America's smaller, lower-quality credits. Now it has a lock on that market" (Institutional Investor Oct. 1981:217)

Michael Milken, the "father of the junk bond" and the "inventor of Drexel's incredible bond machine" was credited with being the creative genius who made Drexel's success possible.

> Milken...spends 18 hours a day, seven days a week at the controls of a one-of-a-kind, proprietary financing network, better known as the junk-bond market. Impressive as it sounds, to describe Milken as the creator of the fast-growing $100 billion market in low-rated corporate bonds is to understate both his accomplishment and his influence. (Business Week July 7, 1986:56)

Mergers and acquisitions The use of mergers and acquisitions was widely used as a competitive strategy in many industries between 1975 and 1990. The securities industry was no exception, as evidenced by Prudential Insurance Company's acquisition of Bache Securities, and Sears, Roebuck & Company's purchase of Dean Witter Reynolds, Inc. (Business Week Jan. 16, 1984:66), as well as the long string of mergers and acquisitions precipitated by the American Express acquisition of Shearson Loeb Rhodes in 1981

(Time March 22, 1993:25). In the articles surveyed, there are 14 mentions (10%) of Merrill Lynch mergers and acquisitions, four mentions (9%) of Charles Schwab, and Drexel Burnham is mentioned twice (1%).

One of the most widely publicized Merrill Lynch mergers was its deal in 1982 with Hong Kong businessman Fung King Hey. At that time few Americans had heard of Fung King Hey, but Merrill Lynch felt he might be the key to open strategic doors in international trade.

> The deal linked up financial heavyweights from three continents in what Fung calls a trilateral relationship. Merrill Lynch bought substantial stakes in two of Fung's companies: 25% of Sun Hung Kai Securities, the brokerage, and 15% of Sun Hung Kai Bank...Brokerage and bank thrive on Fung's web of regional connections, extending from gold buyers in Indonesia to government leaders in the People's Republic of China. Merrill Lynch embraced Fung mainly for his links to the most affluent investors in Southeast Asia--the overseas Chinese...Acting on its own, even sophisticated, resourceful Merrill Lynch would be unable to gain their loyalty, which must be cultivated through personal and cultural bonds. (Fortune Aug. 23, 1982:165)

After spending $80 million in May, 1982, to buy into Sun Hung Kai Securities, "Hong Kong's premier stock brokerage", and its affiliated bank, Merrill Lynch spent another $5 million in 1983, after sharp drops in profits of the bank and brokerage firm. Merrill Lynch officials insisted that this increase in ownership fit Merrill's "long term strategy to modernize a classic Chinese family-owned business", and asserted that the advantages of the merger

"far outweigh any temporary problems" (Business Week Oct. 17, 1983:116). Although the Fung King Hey merger was described as being an adventure full of "thrills and spills", Merrill Lynch remained optimistic. In 1985 company officials stated that Fung's business connections were "more important than we ever imagined in making the investment", characterizing Fung's relationships around Asia as "unique and irreplaceable" (Fortune July 8, 1985:122).

Other Merrill Lynch acquisitions included a brokerage firm in 1978 and another in 1984. In 1978 Merrill Lynch acquired White Weld, a small privately owned brokerage firm that had shown operating losses of $4.3 million the previous year. White Weld had a substantial network of stockbrokers and an "impressive" corporate finance department. Merrill Lynch Chairman, Donald Regan, asserted that the acquisition was "one of the best bargains in Wall Street history" (Fortune Oct. 23, 1978:90).

In 1984 Merrill Lynch was in the process of reorganization and had experienced "unprecedented losses", but according to a Merrill insider the acquisition of A. G. Becker Paribus, Inc. was "simply too good a deal to pass up". Becker, the U. S. securities unit of a French bank, was strong in a number of areas considered advantageous to Merrill Lynch, including corporate finance, fixed-income trading, and commercial paper (Business Week Aug. 20, 1984:133).

Becker's retail equity brokerage business was excluded from the Merrill Lynch purchase. Retail offices were sold to other firms on an individual basis. The two mentions of Drexel Burnham pertaining to mergers and acquisitions have to do with the firm's acquisition of three offices of Becker Paribas-- Chicago, Los Angeles, and Puerto Rico. (Wall Street Journal Aug.21, 1984:12; Wall Street Journal Aug. 24, 1984:3).

The first of the four articles in this category that mentions Charles Schwab & Company is a 1981 article stating that the California based discounter "has a jump on attracting clients" through the acquisition of the New York based brokerage firm, Kingsly, Boye & Southwood. Inc. This was an obvious move by Schwab toward broader geographic coverage (Wall Street Journal Aug. 5, 1981:21).

The other three articles on Schwab mergers and acquisitions pertain to the management led leveraged buyout of the firm from BankAmerica in 1987. A leveraged buyout occurs when a company borrows money to make an acquisition, pledging the assets of the acquired company to cover the loan (Securities Industry Association 1992:129).

When BankAmerica announced in late 1986 its willingness to sell Schwab, Mr. Schwab immediately expressed an interest in buying the firm. In fact, during the strained three-year association with BankAmerica he had not hidden his "interest in wanting to buy back the firm". Mr. Schwab also indicated

his opposition for the sale of the firm to another bank. One of his "great frustrations at BankAmerica" had been federal banking laws that restricted "the range of products and services the brokerage can offer as long as it is owned by a bank" (Wall Street Journal Nov. 7, 1986:7).

ADOPTION OF CHANGING TECHNOLOGY

Responses to changes in technology are divided into three areas: (1) information services, (2) program trading, and (3) market services. Each area is analyzed in terms of reports of adoption of the technology by the firm. Only 36 of the 424 cases (9%) pertain to this category. Table 4.4 indicates the differences among the three companies in number of cases mentioning technology.

In the 235 cases pertaining to Drexel Burnham, there is only one mention (1%) of information technology and one mention of program trading, with no mention of market technology. Merrill Lynch has 20 (14%) mentions of information technology, one case (1%) pertaining to program trading, and five mentions (3%) of adoption of market technology. Charles Schwab has five cases (11%) concerning with information technology, three mentions (7%) of market technology, and no mentions of program trading.

TABLE 4.4

ADOPTION OF TECHNOLOGY
FREQUENCIES AND PERCENTAGES: BY FIRM
1975 - 1990

Type of Technology	Drexel Burnham n (%)	Merrill Lynch n (%)	Charles Schwab n (%)
Information	1 (1)	20 (14)	5 (11)
No Mention	234 (99)	125 (86)	39 (89)
TOTALS	235 (100)	145 (100)	44 (100)
Program Trading	1 (1)	1 (1)	-0-
No Mention	234 (99)	144 (99)	44 (100)
TOTALS	235 (100)	145 (100)	44 (100)
Market	-0-	5 (3)	3 (7)
No Mention	235 (100)	140 (96)	41 (93)
TOTALS	235 (100)	145 (100)	44 (100)

Sources: Wall Street Journal
Business Week
Fortune
Institutional Investor

Information Services

This category includes use of technology to facilitate speed and accuracy of both client account information and stock price data for brokers and/or clients. The years between 1975 and 1990 involved rapidly increasing computer technology, resulting in computerized customer accounts and stock prices now being reported on computer screens. This technology offered the possibility of readily available information for both stockbrokers and clients. A 1985 article asserts that "the delivery of computerized market information is emerging as the hottest sector" of the securities industry (Wall Street Journal June 19, 1985:33).

> Among other features, the new systems electronically maintain each broker's book, or customer-account records. This information is then presented in ways that allow the broker to easily summon a comprehensive overview of a customer's portfolio, making it easier to spot opportunities for shifting exposures to risk, to see if income goals are being met and to highlight problems (Wall Street Journal July 29, 1987:17).

Merrill Lynch was a leader in the adoption of sophisticated information systems for its brokers. The firm's most ambitious and widely publicized move into information services was Merrill Lynch's joint venture with IBM for the delivery of stock-quote and financial data to IBM desktop computers. Articles concerning this joint venture are coded as information technology because of the stated purpose of delivering "a powerful new tool to stockbrokers" which would begin by "equipping Merrill

Lynch's 10,000 account representatives with the new units" (Business Week April 1, 1984:38). A Merrill Lynch spokesperson stated: "clearly our plans are to make this Merrill Lynch's major information network" (Wall Street Journal March 22, 1984:8).

The new information system allowed stockbrokers to divide the screen into multiple sections to display information such as the latest trades, client accounts, or news services. Machines could also be programmed to alert stockbrokers when certain stocks hit new highs or lows, as well as display a list of all the clients who own the stock. A Merrill Lynch vice president proposed that the new system would "make the money manager of today the information manager of tomorrow" (Business Week April 1, 1984).

The plan included the eventual marketing of the service to brokerage firms, banks, and thrift institutions. Ultimately, individuals with IBM Personal Computers were expected to have access to limited quantities of the information. When the joint venture, International Marketnet, was closed three years later, sources close to the undertaking indicated that the system, which promised to go beyond other financial data services, was also more costly than other services. When the closing was announced in January of 1987, the system was termed costly and complicated, and still had few users, even within Merrill Lynch (Wall Street Journal Jan. 2, 1987:2).

Many of the 20 mentions of Merrill Lynch's use of information technology pertain to this joint venture. Therefore, since the bulk of information technology cases involve International Marketnet, the failure of this strategy greatly limits evidence of adoption of information technology as a factor in variation in deprofessionalization.

Within weeks after the announced closing of International Marketnet, Automatic Data, a New Jersey based computing services concern, announced an agreement to develop a customized quote-service system for Merrill Lynch. Although Merrill's contract with the top-ranked Quotron Systems, Inc. ran through 1989, the firm was obviously still seeking better ways of delivering stock price quotes and financial information to its brokers. A Merrill Lynch spokesman said the company "has been looking and continues to look for highly advanced data gathering information machinery for its 10,000 brokers" (Wall Street Journal Jan. 14, 1987:28).

Not only did Merrill Lynch attempt to improve information services for its brokers, it also worked to provide more information to its clients. Along with other major retail brokerage firms, Merrill Lynch recognized the importance of offering customers up-to-date account information "as a way to please favored clients and attract new ones". Merrill developed a system to deliver up-to-the-

minute analysis of client portfolios at the broker's request. For the most part, these services were reserved for accounts with "broadly diversified holdings or substantial trading activity", but could also be used as "marketing tools to lure new accounts (Wall Street Journal July 29, 1987:17). Use of the services were at the broker's discretion.

Merrill Lynch has also made information and broker access available to clients with limitations or special needs. The firm provides a separate 800 number to aid hearing impaired clients, and deaf investors can consult with a broker by using a computer system that operates similar to a cash machine (Wall Street Journal Feb. 22, 1990:A1).

Charles Schwab & Company also demonstrated a strong interest in information services for their brokers and customers. Schwab brokers handle orders randomly as they come in, an approach that "hinges on using advanced computer systems to provide handy access to customer accounts" (Business Week May 12, 1986:82). Since customers make unassisted trading decisions, information services for customers are also vital for success in discount brokerage.

In 1985 Schwab introduced an electronic information service consisting of three products:

> SchwabQuotes is an automated stock quotation and news service that is accessible over any TouchTone phone by dialing a local number. An

> audio news feature of the service, provided by Dow Jones & Co., will supply news on more than 6,500 individual companies and on 100 categories of industrial, business, financial and general interest information. Two software programs--"the Equalizer" and "Financial Independence"...let users review their portfolios and receive trade confirmations, commissions data and electronic mail. It also provides portfolio management, market commentary...and access to the Dow Jones News/Retrieval service (Wall Street Journal Feb. 27, 1985:20).

In 1987 Schwab reaffirmed the importance of information services for brokers and customers when it installed a new mainframe computer and announced plans to double telephone capacity within six months (Business Week Nov. 23, 1987). Schwab's Equalizer system allows investors to trade stocks at home, but the firm expanded its electronic business in 1989 when Schwab's "discount brokerage and investment information services became available on an at-home computer system called GEnie". At the time Schwab joined the system it had more than 167,000 subscribers in the U. S., Canada and Japan (Wall Street Journal Sept. 22, 1989:C1). In 1990, when an "increasing amount of Schwab's revenue" was coming from electronic services and software, the company introduced a Telebroker service that allowed investors to get market quotes and place orders by using a push button telephone (Business Week March 19, 1990).

Only one of the articles pertaining to information services mention Drexel Burnham. This is a short article announcing that MCI Communications Corporation had received

a three year contract to provide telecommunications services to Drexel Burnham (Wall Street Journal Nov. 1, 1989:A6).

Program Trading

The second type of technology involves program trading, which describes a wide range of trading strategies, all of which involve the purchase or sale of a group of fifteen or more stocks. There are only two mentions of program trading, one for Drexel Burnham and one for Merrill Lynch.

This type of computer-assisted securities trading has been quite controversial. On one hand, it created the possibility of trading a large group of stocks in a way that was much less time consuming and labor intensive than previous methods. However, program trading, especially stock index arbitrage, has also been viewed as dangerous, because it increases the volatility of the market. Index arbitrage is a strategy in which "millions of dollars of stocks and stock-index futures are bought and sold in quick bursts, to capitalize on tiny price differences between the two markets" (Wall Street Journal Aug. 29, 1989:C1)

Although Merrill Lynch was listed as being among the fifteen most active program trading brokerage houses in 1989, the firm announced in 1990 that it would "continue its policy of refraining from stock index arbitrage trading for itself and for its clients until the firm decides that proper regulations are in place to address excess

volatility" (Wall Street Journal June 14, 1990:8A). In 1989 Drexel Burnham indicated it would "plunge" into certain types of program trading, but also indicated it would limit its trading to non-arbitrage activity such as "rapid restructuring of portfolios by buying or selling huge blocks of stock (Wall Street Journal Aug. 29, 1989:C1).

Since there are only two mentions of program trading, it seems that companies either kept a low profile about their involvement in program trading, or this involvement was not considered "newsworthy" by the business press. Other sources indicate that program trading stirred up a good deal of controversy during the period covered by the study (see Neubert 1986; Essinger 1990; Furbush 1990), but it seems that the involvement of particular firms seldom became a part of the debate.

Market Services

Technology coded in the category of market services includes changes, other than program trading, involving placing and execution of orders. This type of technology can be carried directly to the customer, which is the focus seen in Schwab articles. The Schwab Equalizer program, the GEnie computer system, and the Telebroker service not only brought information to customers, but are also examples of the discounter bringing simple and direct placing of orders to as many customers as possible.

Articles coded in the category of market services technology also include automated systems used by brokerage firms to execute trades of OTC (over-the-counter) stocks or stocks not listed on the New York Stock Exchange. Merrill Lynch was a leader in the development and use of automated systems. In 1979 the firm announced it had developed an electronic system that would allow it to "find the best market for a customer's trade and send the trade to that securities market in a fraction of a second" (Wall Street Journal Sept. 24, 1979:2). Although technically this system was not limited in terms of order size, Merrill indicated that it would not be used for "multithousand share orders" that could have an impact on market price of stocks. Orders of this type would continue to be handled by Merrill Lynch traders, who arrange large transactions.

In 1982 Merrill started another innovation. A series of computer link-ups put Merrill brokers in touch with the firm's commercial paper traders in New York. This meant that "quotations of prices on the paper are available on the brokers' terminal screens, and order entry systems are in place" (Wall Street Journal Sept. 7, 1982:44).

By the mid-1980s a number of brokerage firms, including Merrill Lynch, installed automated systems which enabled customers "to have an OTC order confirmed almost instantaneously", and were expected to "dramatically cut errors and long delays common in heavy trading periods"

(Wall Street Journal Jan. 11, 1985:6). Although Merrill was involved in a number of innovative projects, it "adamantly draws the line at handing customers the ability to make investment transactions electronically" (Business Week Jan. 16, 1984).

Overall, there were only 36 (9%) mentions of adoption of changing technology. Of these, mentions of information technology account for 6 percent (26 mentions) of the 424 cases. Since the failed Merrill Lynch/IBM venture was mentioned in the majority of Merrill Lynch's articles concerning information technology, evidence of the impact of information technology on variation in deprofessionalization is even less than indicated by the 26 mentions of information technology.

When mentions of the failed Merrill Lynch strategy are disregarded, this leaves Schwab with the greatest percentage (11%) of mentions of information technology. Since Schwab brokers do not serve a particular group of customers, but simply take the next phone call, information services are especially important for them. Also, since customers make investment decisions, it is advantageous to Schwab to get as much information as possible to clients. Schwab also has the largest percentage (7%) of mentions of market technology. Once again, this is in keeping with their emphasis on customers being able to place their orders as easily as possible.

SCANDALS

Responses to scandals are analyzed by types of scandals in which firms were involved as well as by whether or not the firm responded to the scandal by offering a solution to be carried out by the company.

Six types of scandals are analyzed: (1) Insider trading, (2) Junk bond fraud, (3) Other type fraud, (4) Multiple types, including insider trading, (5) Other multiple types, (6) Churning.

Clearly, the categories pertaining to scandals are mentioned more frequently than any other group of categories in the study. As shown in Table 4.5, 262 cases (62%) of the 424 cases mentioned some type of scandal. Of these 262 cases, 205 (78%) mentioned Drexel Burnham, 50 (19%) mentioned Merrill Lynch, and eight (3%) mentioned Charles Schwab.

Drexel Burnham is the most frequently mentioned firm with 21 mentions (9%) of insider trading, ten mentions (4%) of junk bond fraud, and 20 mentions (8%) of other type fraud. Multiple types of fraud that include insider trading accounted for 57 percent (133 mentions) of Drexel Burnham's 235 cases, and there are 21 cases (9%) of other multiple frauds. There were no mentions of churning.

TABLE 4.5

TYPES OF SCANDALS
FREQUENCIES AND PERCENTAGES: BY FIRM
1975 - 1990

Types of Scandals	Drexel Burnham n (%)	Merrill Lynch n (%)	Charles Schwab n (%)
Insider Trading	21 (9)	10 (7)	-0-
Junk Bond Fraud	10 (4)	-0-	-0-
Other Type Fraud	20 (8)	26 (18)	4 (9)
Multiple with Insider Trading	133 (57)	3 (2)	-0-
Other Multiple	21 (9)	8 (5)	3 (7)
Churning	-0-	3 (2)	-0-
No Mention	30 (13)	95 (66)	37 (84)
TOTALS	235 (100)	145 (100)	44 (100)

Sources: Wall Street Journal
Business Week
Fortune
Institutional Investor

There are ten mentions (7%) of insider trading pertaining to Merrill Lynch, no mention of junk bond fraud, and 26 mentions (18%) of other type fraud. There are three mentions (2%) of multiple fraud including insider trading, eight mentions (5%) of other multiple types of fraud, and three mentions (2%) of churning.

Charles Schwab is the least frequently mentioned firm in the scandal categories, with mentions in only two of the six categories. There are four cases (9%) of single type fraud (other than insider trading and junk bond fraud), and three cases (7%) of multiple types of fraud.

Insider Trading

Insider trading refers to buying or selling securities on the basis of information not readily available to the general public. Insider trading makes for exciting headlines, particularly in the late 1980s when there was a rash of insider trading scandals that involved millions of dollars. For many people, this practice has come to symbolize unethical business behavior in the securities industry. It is "probably the most flagrant securities law violation" (Business Week Jan. 9, 1989:35). Because insider trading is considered one of the most serious offenses related to securities industry scandals, it is identified in two categories: insider trading, and multiple causes including insider trading.

Twenty-one cases of insider trading as a single cause of scandal pertain to Drexel Burnham and ten mention Merrill Lynch. There are no mentions of Charles Schwab in this category.

From the beginning, Drexel Burnham was involved in what developed into the "biggest insider-trading case in history". In May of 1986 Dennis Levine pleaded guilty to four felony counts related to insider-trading. Levine, who proved to be one of the key players in insider-trading scandals, was a managing director at Drexel Burnham at the time of his arrest. (Wall Street Journal July 8, 1986:3). A few months later Ivan Boesky, a former Drexel client, also pleaded guilty to insider-trading crimes, and senior Drexel officials were served grand jury subpoenas in a continuing investigation of Wall Street's "deepening insider-trading scandal" (Wall Street Journal Nov. 21, 1986:2). Market professionals feared that what began with Levine, who was apparently the "ringleader of the largest insider-trading conspiracy in history, would "soon shake Wall Street's very foundations" (Wall Street Journal Nov. 17, 1986:1).

Several of the articles linking Merrill Lynch with insider-trading pertain to a claim that two Merrill brokers in New London, Connecticut traded on tips about articles to be published in Business Week. Information was supplied by workers in the printing plant that prints the magazine. The trading was discovered when Professional Investor Report

analyzed 20 stocks mentioned by the magazine column, and found that at least eight of the stocks had "risen sharply, sometimes on unusually steep volume, the day before Business Week published positive news" (Wall Street Journal July 28, 1988:3).

In another case two former Merrill Lynch employees were charged with trading on information that they received indirectly from Dennis Levine. This was the first suit in which the SEC filed insider-trading charges against traders who "piggy-backed" on someone's insider trading. It was the stock transactions of these two investors that led the SEC to its investigation of Mr. Levine (Wall Street Journal Aug. 8, 1989:A2).

Junk bond fraud

Although junk bonds are frequently mentioned in connection with security industry scandals, in and of themselves, junk bonds are seldom mentioned as a cause of scandals. Only ten cases make the direct link between junk bonds and scandal; all of these cases pertained to Drexel Burnham. Several mentions of junk bond fraud came early in the Levine/Boesky investigation when federal authorities announced they were "busily probing the inner working of Drexel's junk-bond operation" (Business Week Dec. 22, 1986:18), probing Drexel's "entire junk-bond operation" (Business Week Dec. 1, 1986:31), or "targeting" Drexel in "an intensifying probe focusing on Drexel's high-yield junk

bond operations" (Wall Street Journal Nov. 19, 1986:3). Junk bonds became a focus again in 1990 when investigators questioned the possible link between junk bonds and "America's latest financial scandal--the savings and loan debacle" (Business Week May 7, 1990:35).

Problems having to do with junk bonds are likely to relate to charges such as failing to inform clients of the extent of risk, indicating that the crucial issue is not the junk bonds per se, but irresponsible or unethical behavior related to selling or trading of the bonds. Although Michael Milken was the center of speculation about junk bonds for a number of years, "neither the original indictment nor the offenses to which Milken pleaded guilty involved junk transactions" (Business Week May 7, 1990:37).

Other Types of Fraud

Insider trading and involvement with junk bonds are more flagrant than other types of scandals, but much of the illicit behavior in the securities industry during the period of this study involved serious, but more mundane issues. Other types of fraud include providing false and incomplete financial advice, mail fraud, unauthorized trades, conspiracy to manipulate prices and "front running", which is disclosing the possibility of a customer order to a trader before the trade is entered in the trading pit. "Prior knowledge of a big pending order can enable traders

to profit from the market effect of the order" (Wall Street Journal June 22, 1990:C14).

An example of fraud other than insider trading or junk bonds is seen in widely publicized class action suits charging Merrill Lynch and other brokerage firms with misrepresenting Baldwin-United single premium deferred annuities as risk-free investments. Merrill Lynch was also charged with failing to disclose to two Michigan towns the risks involved in an arbitrage strategy used in the purchase and sale of U. S. treasury notes for police and fire retirement systems. The strategy resulted in losses of about $1.3 million, which Merrill absorbed (Wall Street Journal Dec. 29, 1978:6).

Of the four articles pertaining to Charles Schwab in this category, three have to do with charges of unauthorized trading, which was brought to light by a Business Week article, "Did Schwab Play Fast and Loose with its Customers' Shares?"(Nov. 7, 1988:159). It was found that Schwab did realize gains by "improper use" of customer securities. This unauthorized trading occurred when customers' holdings were subject to partial tender offers, warrants, or conversions. Profits were made in these transactions, but not passed on to customers. Profits from transactions dating back almost four years were at first estimated to be $1 million to $2 million, but later proved to be more (Wall Street Journal Nov. 10, 1988:C9).

Multiple Types of Fraud

Including Insider Trading

Multiple types of fraud are more commonly reported as causes of scandal than a single type of fraud. Often charges of insider trading are linked to other types of fraud. This can be seen in Table 4.5 which shows that Drexel Burnham, the most frequently mentioned firm concerning scandals, is mentioned in 21 cases (9%) concerning insider trading alone and in 133 cases (57%) concerning multiple types of fraud which includes insider trading, bringing the total of these two categories to 66 percent of all Drexel Burnham cases.

Other Multiple Types of Fraud

Not only is insider trading frequently linked to other types of fraud, but in cases that do not involve insider trading, multiple types of fraud are often involved. Multiple types of fraud which do not include insider trading are mentioned in 21 cases (9%) for Drexel Burnham, eight cases (5%) for Merrill Lynch and four cases (9%) for Charles Schwab.

An example of multiple charges is a lawsuit against fourteen firms, including Drexel Burnham and Merrill Lynch, by the city of San Jose, California over a $60 million bond trading loss. The city charged negligence, breach of fiduciary duty and excessive trading in violation of federal securities laws (Wall Street Journal Sept. 25, 1984:45).

Churning

According to the Harvard Law Review, "the 'churning' of a securities account occurs when a dealer, acting in his own interests and against those of his customer, induces transactions in the customer's account which are excessive in size and frequency in light of the character of the account" (Feb. 1967:869). Although this practice has more potential harm for individual investors than many other unethical or illegal practices, it is usually handled within the firm, and with little or no notoriety.

When there is a customer complaint of churning, it is investigated immediately by a company compliance officer. If the investigation indicates a valid complaint, a settlement is often made between the company and the customer. If this is not done, the case is settled through arbitration. The client agreement forms of most brokerage firms include a statement that controversies between company and client will be settled through arbitration rather than being taken to court. Although this clause may occasionally be waived, it accounts for the fact that churning complaints are seldom made public (Hodges 1994).

Only three cases mention churning. All three articles pertain to Merrill Lynch. One article notes that a federal court jury awarded a Florida man more than $371,000 when he charged that excessive trades in his account had reduced the value of the account from $61,000 in 1977 to $4,745 in 1980.

The award was made in spite of the finding that the client was also guilty of negligence in management of his finances, since he was in the broker's office almost daily and controlled what was done with the account (Wall Street Journal Aug. 24, 1983:46).

The other two articles concern charges of excessive trading over a period of two years, although the value of the account rose 50 percent during that time. Merrill appealed but the appeals court awarded punitive damages of more than $2 million (Wall Street Journal May 5, 1987:20; Wall Street Journal June 18, 1990:13C).

Company Indicates Solution

In some cases organizational response to scandals not only includes involvement in scandals, but also the response of offering a solution that could be carried out by the firm. Only one percent (2 cases) of Drexel Burnham scandal cases mention the firm offering a solution, while 22 percent (11 cases) of Merrill Lynch's cases that involved scandals indicate a company solution. All of the seven cases mentioning Schwab scandals indicate a solution offered by the firm.

However, these numbers fail to give a clear indication of the timing and nature of solutions offered by Merrill Lynch and Charles Schwab.

Merrill Lynch seems to have been particularly adept at moving quickly and decisively to lessen the effects of

scandal by offering a solution. In February of 1987 a Wall Street Journal article reported that because of the "spreading insider-trading scandals", Merrill Lynch considered takeover speculations too risky. Therefore they had brought their arbitrage group more under the control of the "traditional stock-trading operation". They also announced that Mr. Timothy Tabor, who had headed the operation for about eight months, planned to leave the firm. A Merrill spokesman said Merrill "began putting its new lower risk arbitrage investment strategy into place at the beginning of the year" (Feb. 4, 1987:3). An article a month later concerning risk arbitragers and corporate takeover abuses listed Timothy Tabor as one of those arrested. It was noted that "until recently" he was head of Merrill's arbitrage operation. (Wall Street Journal Feb. 4, 1987:3).

The scandal involving the sale of Baldwin annuities was one of the most widely publicized instances of Merrill Lynch attempting to provide a solution for customers. After Baldwin-United Corporation declared bankruptcy, customers began lawsuits against Merrill Lynch and other brokerage firms that sold the annuities. Merrill was said to be "pioneering again" when the firm, even though it had no legal obligation to do so, set aside $88 million as a partial reimbursement for its customers who bought Baldwin annuities. A 1984 article states: "Merrill's decision to provide massive refunds so early in litigation may be

unparalleled in securities industry history" (Business Week Feb. 6, 1984:22). One of the attorneys handling several suits against Merrill depicted the firm's action as "an indication that Merrill Lynch is very concerned about its liability" (Business Week Feb. 6, 1984:23).

Several articles also mention Schwab's repayment of $3.5 million, with interest, to customers. This represents refunds for unauthorized trading (Wall Street Journal Nov. 10, 1988:C9).

Merrill Lynch moved aggressively and quickly to make massive refunds before their legal responsibility was decided. On the other hand, Schwab announced refunds only after investigations showed extensive unauthorized trading. These investigations indicated unauthorized use of customers' shares, rights, and warrants over a period of several years (Wall Street Journal Oct. 31, 1988:C23). Even when refunds were announced Schwab seemed to try to sidestep responsibility by indicating that refunds were for gains that "may not have been appropriate" (Wall Street Journal Nov. 10, 1988:C9).

These two examples illustrate that all attempts to solve problems and enhance a company's reputation may not be equally successful in building trust. Even though the percentage of mentions of a company indicating a solution was higher for Schwab (100%) than for Merrill Lynch (22%),

the Merrill articles seem to be more favorable for the company's reputation.

SUMMARY

As expected, the three firms differ in their movement into new areas and in their choices of competitive strategies. Merrill Lynch was more involved in movement into a number of new areas than the other two firms. In keeping with the diversity offered by this movement into new areas, Merrill Lynch also chose the competitive strategy of providing full service more often than other strategies. Drexel Burnham used the strategy of establishing a special market niche, in this case trading junk bonds. This niche was established early in the period and maintained until the time of the firm bankruptcy early in 1990. Because of the choice in 1975 to take advantage of the competitive rate structure by establishing a discount brokerage firm, Charles Schwab & Company used low cost as its primary competitive strategy. An unexpected finding is that there are also five mentions (11%) of Charles Schwab in connection with providing full service.

Only 36 of the 424 cases (9%) mention adoption of technology, with 26 of these pertaining to Merrill Lynch. This percentage is even lower if mentions of the failed joint venture of Merrill Lynch and IBM are disregarded. Charles Schwab would then have the greatest percentage of

its cases mentioning both information (11%) and market (7%) technology. Adoption of information technology is in keeping with Schwab's need of information for brokers who handle accounts on a random basis, and for customers who make investment decisions. Market technology is also needed by discount brokers so that customers can place orders.

There are two possible explanations for the overall low percentage of cases mentioning technology and the relatively high percentage of Schwab cases in this category. These explanations deal with impact versus interest. It is possible that technological changes had a relatively low impact on deprofessionalization of stockbrokers. However, this aspect of the brokerage industry may simply be of lesser interest to business news writers. It may be that the Schwab references indicate greater impact on deprofessionalization because they relate to a shift of power from professionals to clients. On the other hand, business news writers may have judged these client-related technological changes to be of greater interest to their readers.

Mentions of involvement in scandals are more numerous than any other category, with 62 percent (262 cases) of the 424 cases identifying involvement in scandals. Not only is this the most frequently mentioned category, but there are also more differences among the three firms. Drexel Burnham is by far the most frequently mentioned firm concerning

scandals. Sixty-two percent of the 424 cases involve mention of scandal, with 78 percent of these mentioning Drexel Burnham. Mention of some type of scandal occurs in 205 (87%) of Drexel's 235 cases. Thirty-four percent (50 cases) of Merrill Lynch's 145 cases mention involvement in scandals. There are seven Schwab cases (16%) that include mention of involvement in scandals. Not only is Drexel mentioned most often in involvement in scandals, it is mentioned least in offering solutions to problems relating to scandals. Drexel Burnham's heavy and long term involvement in scandals indicates the likelihood of greater decline in client trust for that firm, and for the stockbrokers within the firm.

In addition to involvement in scandals, there are several other areas in which I expect differences in organizational responses to influence variation among firms in deprofessionalization of stockbrokers. These areas include diversification, choice of low cost strategy, and choice of special niche strategy.

In this analysis, diversification is evidenced by movement into the areas of banking, real estate, and insurance, as well as by the choice of a full service strategy. There are several possible effects of diversification on deprofessionalization. For example, when a firm moves into new services, the role of the stockbroker may lose importance within the organization, especially if

the firm diversifies but the brokers' professionals tasks are not broadened or enhanced as a part of the diversification.

However, diversification does not necessarily contribute to deprofessionalization. Diversification may give stockbrokers an opportunity to apply their professional expertise in a broader area. In this case, even though it is an organizational choice, diversification may have a positive effect similar to the effect expected when diversification is a professional choice.

If a firm's choice of low cost strategy results in stockbrokers having employee status rather than professional status, diversification will have virtually no effect on deprofessionalization of stockbrokers within the organization. Since deprofessionalization has already taken place, diversification does not contribute to the process in either a positive or negative way.

Quantitative analysis reveals organizational differences in diversification. However, the overall effect on deprofessionalization can be more accurately assessed by considering diversification within the context of other organizational factors.

Choice of competitive strategy is expected to have a strong influence on variation in deprofessionalization. For example, according to strategic choice theory, choice of a low cost strategy is likely to involve cutting costs by

lowering wages. Companies pursuing a cost-reduction strategy tend to rely on workers who focus on quantity of output rather than quality, avoid taking risks, avoid seeking greater responsibility, and behave in relatively repetitive and predictable ways (Schuler et. al. 1987:19). Since these qualities are inconsistent with professional characteristics, I would expect choice of this strategy to contribute to deprofessionalization.

Although choice of a special niche strategy is not as clearly detrimental as the low cost strategy adopted by Charles Schwab & Company, deprofessionalization of stockbrokers is likely to increase within a firm making a special niche strategy choice. If the niche chosen is successful, it can create a competitive edge and bring financial success for the firm. However, shifts in resource allocation to support the special niche established by the company may result in loss of interest for and support of other areas within the organization. This shift in focus could contribute to deprofessionalization for professionals outside the chosen niche..

Using the descriptive statistics of differences in organizational responses as a starting point, the qualitative analysis in the following chapter gives further insight into the relationship between differences in organizational responses and variation in deprofessionalization. I will use the empirical data from

the 412 articles along with concepts of deprofessionalization and strategic choice theory to determine what effects, if any, differences in organizational responses had on variation of deprofessionalization in the brokerage firms of Drexel Burnham, Merrill Lynch and Charles Schwab. I anticipate that environmental changes will not affect professionals in all firms in a uniform way, but will instead be mediated by organizational responses, with the differences in those responses resulting in variation in deprofessionalization.

CHAPTER 5

QUALITATIVE ANALYSIS

Quantitative content analysis answers the first three research questions by indicating differences among Drexel Burnham, Merrill Lynch, and Charles Schwab in terms of their responses to the environmental changes of deregulation, changing technology, and scandals during the period 1975 through 1990. However, my attempt to discover ways in which organizational responses affect the extent of deprofessionalization goes beyond the statistical data of the quantitative content analysis of the previous chapter.

In this chapter qualitative analysis is used to answer the fourth research question: How did differences in organizational responses affect variation among firms in deprofessionalization of stockbrokers? I will use data from the content analysis described in Chapter Four, along with concepts of deprofessionalization and strategic choice theory, to examine the relationship of organizational responses and variations in deprofessionalization in the three firms being studied.

This portion of the study is guided by several questions:

1 - What effects, if any, did organizational responses have on control of work?

2 - What effects, if any, did organizational responses have on content of work?

3 - What effects, if any, did involvement in scandals have on company reputation?

4 - What effects, if any, did company solutions to problems related to scandals have on company reputation?

5 - Did some organizational responses have a stronger effect on deprofessionalization than others?

The first two questions deal with variation in autonomy of professionals. Autonomy, indicated by control and content of work, has been a primary area of concern in studies of deprofessionalization. Organizational employment of professionals is considered an important aspect of deprofessionalization since it suggests a loss of ability to control one's work.

Because trustworthiness of professionals within an organization is linked to some extent to the perceived trustworthiness of the organization, I have included two questions pertaining to organizational reputation. Company reputation is often judged to some extent by positive or negative media representation. Therefore, reports of scandals would be likely to hurt company reputation, while company efforts to solve problems would be expected to help company reputation. Even though organizational responses

are expected to mediate the effects of environmental changes on deprofessionalization, all responses are not expected to have similar effects on deprofessionalization. Therefore, the last question explores not only differences in organizational responses, but also differences in the effects of these responses on deprofessionalization.

CHARLES SCHWAB & COMPANY

Charles Schwab & Company is a good example of the extensive influence that choice of a certain competitive strategy can have on deprofessionalization. The firm chose cost reduction as its primary strategy to deal with the increased competition that resulted from the deregulation of the securities industry.

Control and Content of Work

Lowering wages is one of the primary methods that firms use when implementing a low cost strategy. For Schwab this meant employing stockbrokers as salaried employees, rather than as professionals who received direct compensation for their services to clients.

Not only were Schwab stockbrokers deprived of compensation on a fee for service basis, but the company system limited the advantages inherent in professional licensure. States and stock exchanges require brokers to be licensed in order to take customer orders and place these orders with an exchange. Licensing is considered a part of

the professionalization process because it indicates control over who can enter the profession, and also indicates recognition of professional expertise by licensing agencies outside the profession. However, being a licensed professional without the control of one's work makes licensure less meaningful.

Control of work is eroded by a disregard for professional knowledge and expertise. In order to deliver services at rates 30 percent to 70 percent lower than full service brokerage firms, Schwab chose a system that eliminated the availability of investment advice for clients. Professional knowledge and expertise in financial matters, leading to sound investment advice, are key aspects in the professional status of stockbrokers. However, because Schwab chose the cost reduction strategies of employing stockbrokers as salaried employees and limiting services, this professional knowledge is neither expected nor available to clients. Schwab's clients "make their own investment decisions and want cheap commission rates, not investment advice" (Wall Street Journal May 3, 1989:C1).

Client-broker relationships are "deliberately depersonalized" at Schwab. Brokers do not choose their clients. In fact, they are not even assigned their own accounts. Instead, they simply "handle orders randomly as they come in" (Business Week May 12, 1986:82). The absence of broker-client relationships and lack of respect for

professional expertise was not without problems for the firm. Some Schwab clients complained that this "impersonal, high-volume approach" resulted in long "on-hold" waits on the phone as well as "brusque treatment" (Wall Street Journal April 4, 1980:9). In an effort to create more credibility and offset the impersonal image, Schwab initiated ads inviting investors to contact Mr. Schwab personally, an invitation that was likely to backfire since Charles Schwab was usually unavailable. A former midlevel manager of the firm commented that "when you tried to call him, you'd get put on hold twice and then get a recorded message" (Business Week May 12, 1986:81). In spite of these problems, the firm did nothing to change the random handling of orders by stockbrokers.

During the time period between 1975 and 1990, Schwab moved into some new areas in an attempt to become similar to full service brokerage houses. In 1985, after almost ten years as the country's leading discount brokerage firm, the founder of Charles Schwab & Company expressed his interest in "becoming more and more mainstream" (Institutional Investor Sept. 1985:284). Eighteen percent of the Schwab articles included in this study mentioned movement into new areas and eleven percent related to use of full service as a competitive strategy. Although these percentages are considerably lower than the 41 percent of Schwab cases that indicated low cost as a competitive strategy, they do

indicate an interest in moving beyond the narrow confines usually associated with discount brokerage.

Yet, a Schwab senior vice president posed this question, "If business is so fabulous, why are we introducing all these new products?" (Institutional Investor Sept. 1985:283). At least two answers are suggested for this question. First, in an increasingly competitive market, narrowly focused discount firms face the possibility of clients leaving simply because another firm offers a lower price. Second, without the "stimulating force" provided by the broker-client relationship, it is felt that "discounters' customers inexorably slide into lethargy" (Institutional Investor Sept. 1985:283). New products and services could stimulate new interest for these lethargic customers.

Schwab attempted to change its image from "discount broker" to "off-price financial-service company" by offering more products and services. As this was done, the firm also raised brokerage fees. This was especially true for small trades, where Schwab's charges were sometimes higher than those of full-service brokerage firms (Wall Street Journal Oct. 10, 1988:C1).

In deprofessionalization literature, movement into the jurisdictions of other professions is generally viewed as having the effect of diminishing deprofessionalization within the profession making such moves. However, when the

content of work is changed through organizational rather than professional decisions, the result may not be a lessening of deprofessionalization. The greater diversity of products and services, the elegant offices with "fancy electronic stock-price displays" may have enhanced the image of the company (Fortune Jan. 20, 1986:86), but did not result in professional status for stockbrokers within the firm. In fact, as the company moved into new areas, it emphasized that the policy of no investment advice would continue. Even though their tasks may have changed to some extent, diversification could not be advantageous to Schwab stockbrokers in light of the limitations of their employee role. At Schwab this employee role specified random handling of orders and precluded use of professional knowledge for investment advice to clients, thus denying brokers control of their work and authority over clients.

Effects of Scandals on Company Reputation

Only 16 percent of Schwab cases linked the firm to scandals of any type, compared to 33 percent for Merrill Lynch and 87 percent for Drexel Burnham. Infrequent mentions of Schwab involvement in scandals suggests a good company reputation, which could in turn lead to greater client trust. In addition to a low percentage of cases mentioning scandals, all Schwab scandal articles indicated an effort to solve problems. This combination of low number

of scandal articles along with 100 percent of scandal cases mentioning company efforts to solve the problem involved, suggests little damage to Schwab's reputation from involvement in scandals. However, the content of the most widely publicized Schwab case, along with the way in which the company was organized, indicate positive results may not have been as strong as expected.

The most publicized scandal involving Charles Schwab & Company came to light in late 1988 through articles in Business Week, one of which asked the question, "Did Schwab Play Fast and Loose with its Customers' Shares?" (Nov. 7, 1988:159). Various types of improper trading transactions resulted in gains for Schwab through unauthorized use of customer shares. It was discovered that these practices had been carried out for a period of more than three years, and that knowledge of these activities "may well have flowed up the corporate chain to some extent" (Business Week Nov. 7, 1988:160).

In an interview, Charles Schwab downplayed the charges regarding the usage of customer shares by stating that the firm began an internal inquiry concerning the questionable trades in early October, 1988. He characterized the problem as "money that overzealous employees took for Schwab, but a reasonable customer would conclude he was entitled to" (Wall Street Journal Oct. 31, 1988:C23).

At that time the "worst case" assumption of the amount taken ranged from $1 million to $2 million. Mr. Schwab later said that approximately $3.5 million in refunds would go to customers for gains Schwab took that "may not have been appropriate". (Wall Street Journal Nov. 10, 1988:C9). Mr. Schwab admitted that "some of our people lost sight of our main commitment--our relationship with our customers" (Wall Street Journal Nov. 10, 1988:C9).

The firm's nonprofessional, impersonal broker system could certainly have been a factor in the failure to honor commitment to customer relationships. This situation points out the shortcomings of a system that promotes commitment to clients while precluding broker-client relationships. Thus it becomes more understandable that Schwab employees would seek gain for the company rather than for the client.

The firm exhibited a great deal of reluctance to accept responsibility and to acknowledge the improper nature of their actions. There was broad disparity between Mr. Schwab's conclusion that the trading in question "may not have been appropriate", and statements of SEC officials indicating that it may have amounted to "outright larceny" (Business Week Nov. 7, 1988:159). In spite of this dissimilarity of explanation, the firm's reputation was probably boosted to some extent when Mr. Schwab not only apologized, but also returned the illegal gains to Schwab customers.

Effects of Organizational Responses on Deprofessionalization

Examination of the organizational responses of Charles Schwab & Company reveals some factors ordinarily associated with limitation of deprofessionalization. First, as discussed earlier, Schwab cases suggest a generally good reputation indicated by the small percentage of cases mentioning Schwab's involvement in scandals, along with indications of the company attempting to solve related problems in all cases. Also, during the period 1975 through 1990, Schwab expanded the products and services it offered. This expansion meant a broader scope of work for the brokers in the firm. Expansion also included moving into the jurisdiction of other professions, such as banking and real estate.

Deprofessionalization literature links the crossing of jurisdictional boundaries to gains in power for the profession making that expansion into new territories. Yet, this positive effect for professionals applies to diversification decisions made by a profession, not to those made by an employing organization. In the case of Schwab, there is strong evidence that the choice of a cost reduction strategy had a stronger effect on deprofessionalization than either diversification or minimal involvement in scandals.

The seemingly positive aspects of moving into jurisdictions of other professions, expanding products and

services, and maintaining a relatively good reputation become irrelevant in terms of decreased deprofessionalization because of Schwab's overriding choice of low cost strategy. This strategy reduced stockbrokers to a role of order-taking employees rather than that of financial professionals. Not only did Schwab brokers have an employee status, but under a random system of broker-client contact, stockbrokers and clients remained strangers, a situation associated with increased deprofessionalization.

Strategic choice theory suggests that companies using a cost-reduction strategy need employees with predictable, repetitive behavior, low preference for responsibility, and narrow skill application (Schuler, et. al. 1987:19). These company expectations for employee behavior are not consistent with professional characteristics. Schwab's choice of a low cost strategy set in place a system in which other potentially positive responses were meaningless in the possible lessening of deprofessionalization because stockbrokers did not have professional status in this firm.

DREXEL BURNHAM & COMPANY

There are indications of professional autonomy for brokers within the Drexel Burnham organization. The firm chose a competitive strategy that seemed at first to lead to success for Drexel without apparent increase in

deprofessionalization for stockbrokers in the firm. However, in time the competitive strategy of establishing a special niche led to serious problems for Drexel Burnham & Company and resulted in increased deprofessionalization for stockbrokers in the firm.

Control and Content of Work

Organizational employment does not mean that professionals lose autonomy. Professionals in organizations may, in fact, be able to exercise some control over their work. There certainly seems to be a greater possibility for stockbrokers to control their work within the Drexel Burnham organization than in that of Charles Schwab.

Robert Linton and Frederick Joseph, chief executive officers of Drexel during the period of the study, encouraged a "lack of regimentation" within the organization, and were reportedly wary of anything that "smacks of bureaucracy". Joseph pointed with pride to Drexel professionals who were aggressive, highly motivated, and entrepreneurial, and the firm was known for a corporate culture that prized innovation. A senior executive vice president said, "We try to run this firm like a small business. We delegate enormous authority to people" (Fortune Sept. 3, 1984:90). Drexel Burnham was said to "hire the best, turn them loose, and intervene only when necessary" (Business Week April 1, 1985:51).

These descriptions suggest an organization in which professionals have some degree of discretion and judgment in performing their work. In contrast to Charles Schwab, brokers at Drexel Burnham had their own clients, were paid on a fee basis, and seem to have been relatively free to make decisions in using professional expertise to help their clients.

Areas of work for brokers at Drexel Burnham were consistent with those of other mainstream brokerage firms, and there is no indication that the company attempted to limit or expand the scope of work of brokers. Although there is no indication of attempts to expand jurisdictions, Drexel Burnham seems to have allowed extensive control of work for professions in the organization. This suggests a positive effect in terms of limiting the deprofessionalization of stockbrokers in the firm.

Ability to control their work was later curtailed for stockbrokers in the firm. As a part of their settlement with the SEC, Drexel agreed to have three outside directors who served as an oversight committee and were generally regarded as the "SEC's watchdogs". Overall, professionals in the firm were subject to more bureaucratic controls (Fortune May 8, 1989:91). Not only was control of work restricted during the latter part of the period, but any positive effect of autonomy for stockbrokers in the firm was weakened by other choices made by Drexel Burnham.

Effects of Organizational Responses on Deprofessionalization

Drexel Burnham chose the competitive strategy of establishing a special market niche, in this case junk bonds. Over time, this choice proved to be disastrous for stockbrokers in the organization and for the firm itself. This niche was chosen early in the period 1975-1990, and was maintained as a major emphasis of Drexel Burnham until its bankruptcy in 1990.

Choice of junk bonds as a special market niche did not, in itself, necessarily indicate an escalation of deprofessionalization of stockbrokers within the firm. In fact, in the early years of the study period there may have been some advantages for brokers as the company became more successful and financially secure. In 1981 Drexel was described as a brash firm that chose the special niche of "lower-quality credits", or junk bonds. This choice of competitive strategy resulted in a reported tripling of corporate finance profits between 1977 and 1980 (Institutional Investor Oct. 1981:218).

Drexel Burnham's junk bond trading operation gave them an edge over their competition. "Drexel was never a Wall Street power until it discovered the vast potential of junk bonds" Wall Street Journal Dec. 13, 1985:1). The firm gained a reputation for having special skills in marketing low-grade securities, and Drexel traders earned a reputation

for "consistently standing behind their offerings". In spite of buyers' loyalty, Drexel Burnham's reputation was far from pristine. There were claims from competitors that they were "brash and pushy", and used "terrorist tactics", which earned Drexel professionals the name "killer Dobermans of Wall Street". Yet this negative reputation, which may have come in part from resentment of Drexel Burnham's success, probably had less effect on deprofessionalization than other factors, including the strength of Drexel's commitment to its chosen niche.

Drexel Burnham chose the special niche of junk bonds, and there were early indications of phenomenal success. This success was, in part, the result of decisions concerning resource allocation. "Under the single-minded Michael Milken, Drexel...made a whole-hog commitment in staff, capital and emphasis to the $75 billion market in sub-investment grade debt that no competitor is ever likely to match" (Institutional Investor June 1985:217).

One of the early indications of the firm's "whole-hog commitment" to junk bonds is Milken's move of his whole division to Beverly Hills in 1978. This division, which was called "the Coast", came to enjoy special privileges and achieved nearly total autonomy. Drexel Burnham made concessions to the needs and desires of the junk bond sales and trading group, and large amounts of money went back to them. Heading the list of recipients of both special

privileges and money, was Michael Milken who reportedly had 1985 earnings of $40 million (Business Week July 7,1986:58), and earnings of $550 million in 1987 (Institutional Investor May 1989:108).

There are some implications that can be drawn concerning how this resource allocation affected other professionals within the firm. As junk bond specialists became more important, generalists became less important. As more resources were allocated to those trading junk bonds, fewer resources were available to other professionals in the firm. Reportedly, there was a commonly held sentiment in the company that some of the people in California not only got the firm in trouble, but were paid extravagantly for doing so. Stockbrokers in the firm considered this situation "demoralizing" to other Drexel brokers (Institutional Investor May 1989:108).

In April 1990 economic and legal problems helped to bring about Drexel's decision to sell its entire retail network. This followed extensive compensation guarantees for employees on the coast, aimed at holding top producers in the high yield department. These decisions upheld the firm's commitment to its junk bond operation, and left its other stockbrokers feeling betrayed. However, the sale of the retail brokerage unit resulted not only from decisions concerning resource allocation, but also from the financial

consequences of extensive involvement by the firm in scandals.

Effects of Scandals on Company Reputation

Of the three firms being analyzed, Drexel Burnham was the most extensively involved in scandals. Eighty-seven percent of the articles pertaining to Drexel Burnham linked the firm to some type of scandal. Drexel was related in some way to many of the major financial scandals of the 1980s. This heavy involvement seriously damaged the company's reputation and eroded client trust.

A series of Wall Street scandals began with the arrest of Dennis B. Levine in May, 1986. Levine was accused of making more than $12 million by trading on confidential information. He implicated Ivan F. Boesky, and before the end of the year Boesky agreed to plead guilty to one felony count and pay a fine to settle Securities and Exchange charges of insider trading. Boesky's fine of $100 million was the largest penalty in the history of the SEC (Wall Street Journal Nov. 17, 1986:1). Both men were involved with Drexel Burnham. Levine was a former investment banker with the firm, and Boesky was a longtime client of Michael Milken.

As government investigations pursued the "biggest insider-trading case in history", a major theme emerged: "In every instance known thus far to figure in the government's investigation, the securities firm of Drexel Burnham

Lambert, Inc. played an important role" (Wall Street Journal Dec. 5, 1986:1). Before there was any knowledge of Drexel's guilt or innocence, it was noted that "in the securities business, even a temporary dent in a company's reputation can translate quickly into losses of customers and money (Wall Street Journal Nov. 21, 1986:2). Following the news of grand jury subpoenas, before any charges were made against Drexel or Drexel officials, more than 1,000 of Drexel's 275,000 individual customers called their brokers to withdraw securities and cash (Wall Street Journal Nov. 21, 1986:2). As the scandals increased, Drexel's reputation continued to suffer and client trust continued to decline.

After two years of investigation, the Securities and Exchange Commission charged Drexel Burnham & Company, Michael Milken, and others with insider trading and securities violations (Wall Street Journal Sept. 8, 1988:1). Civil charges by the SEC opened the way for later criminal charges by the Justice Department. In late 1988, in order to avoid racketeering charges, Drexel Burnham & Company agreed to plead guilty to securities fraud, banish Milken from the firm, and pay a $650 million fine (Business Week March 5, 1990:72).

Michael Milken later faced a 98 count indictment, pleaded guilty to six of the charges, and agreed to cooperate fully with the government in its continuing investigation. He also made a $600 million settlement with

the SEC, and was barred from the securities industry for life (Wall Street Journal April 25, 1990:A6).

In an indirect way Drexel Burnham's choice of competitive strategy contributed to deprofessionalization of stockbrokers in the firm. Drexel had chosen the special niche of junk bonds, which in turn led to allocation of resources favoring that part of the company, and, in time, led to extensive involvement in scandals. In the end, other firms were wary of hiring former Drexel people "who may turn out to be tainted" (Institutional Investor May 1989:108).

MERRILL LYNCH & COMPANY

Merrill Lynch & Company is the largest and most financially secure of the three firms being analyzed. In 1980 Merrill Lynch was the number one U. S. brokerage firm based on the strength of its capital positions. Merrill's total capital of $784,245,000 was more than three times as large as that of its nearest rival (Institutional Investor Jan. 1980:7). The firms's size and financial resources seem to have had mixed effects on deprofessionalization of its stockbrokers. Size of the organization suggests more bureaucratic control, yet extensive financial resources indicate more options in meeting competitive pressures, which could mean less deprofessionalization for professionals in the firm.

Control and Content of Work

Problems inherent in a large corporation became apparent after Merrill Lynch's acquisition of the White Weld brokerage firm in 1978. At the time Merrill Lynch had approximately 7,600 stockbrokers and was about ten times the size of White Weld. Because of its size the Merrill organization was more bureaucratic and structured than the smaller firm. Many White Weld brokers resented the bureaucratic red tape and loss of control over their work, and left the firm (Fortune Oct. 23, 1978:84).

While brokers from a smaller firm may have perceived a loss of autonomy when becoming part of the larger organization, Merrill Lynch seems to have allowed a fair amount of autonomy for its brokers. Although they may have had less control of work than brokers at Drexel Burnham, they certainly had a great deal more control than brokers at Charles Schwab. Merrill stockbrokers were able to open and manage their own accounts. Generally, the company did not place limitations on how brokers handled their accounts, and brokers were paid fees based on commissions generated by trades they made in these accounts.

However, there are indications in the Merrill Lynch organization of an ongoing power struggle between the company and its brokers. In 1981 Merrill brokers were reportedly "bristling about all the time they must devote to setting up and servicing money-market fund accounts...for

which they earn no commissions" (Wall Street Journal April 23, 1981:25). Although a Merrill Lynch spokesman said the company does not "encourage brokers to discourage business", some brokers turned away clients who were interested in banking services alone. The company was crossing jurisdictional boundaries to offer banking services, but individual stockbrokers could exercise their autonomy by turning away clients who did not intend to buy and sell stocks or other securities. Brokers were encouraged, but not required, to open money market accounts.

Merrill Lynch was a leader in offering banking services, including its well known Cash Management Account, (CMA). Merrill found this account to be a way of tying clients and brokers more securely to their firm. Clients were enthusiastic about Merrill's CMA, which was the first, and generally considered the best, of this type account. Because of the reputation of its CMA account, the company found that brokers would "think twice about quitting Merrill Lynch for a rival firm" (Fortune April 19, 1982:68). So while brokers were free to refuse to open accounts for banking services, they were, at the same time, enticed by the prestige gained through Merrill offering these services.

Another element of the firm-broker power struggle is evidenced in brokerage firms using litigation to prevent brokers from taking clients with them when they leave the firm. Companies spend a great deal of time and money

training brokers and feel they should be protected from losing clients when brokers leave the firm. On the other hand, stockbrokers think that because they open the accounts, the clients are theirs, not the company's. Merrill Lynch tries harder than most companies to have clients think of themselves as Merrill Lynch clients rather than clients of a particular broker.

Merrill spends a great deal of time and money on litigation, yet does not always win. In one case arbitrators ruled that only those accounts that were assigned to the broker by the company belonged to the company, while the broker was allowed to keep the clients he had acquired on his own (Wall Street Journal April 5, 1984:33).

The company exerted power over brokers by making changes in its compensation system. The new system rewarded brokers for making larger trades, opening margin accounts, and for accumulating customer assets. Before this change brokers could earn as much making numerous small trades as they could making fewer, larger trades. After the change, brokers could still choose to center their business around relatively small trades, but they would earn less because fees were now reduced on these trades. Because large, diverse accounts are more difficult to transfer to another firm, rewarding brokers for increasing customer assets is

likely to tie clients and brokers more closely to the company (Wall Street Journal Feb. 25, 1986:3).

Merrill Lynch later set up bonuses for brokers selling Merrill's in-house mutual funds (Wall Street Journal Feb. 15, 1989:C1), and eliminated commissions on sales of non-Merrill annuities when investors switched from a Merrill product. The company stressed that brokers "have every opportunity" to sell whatever annuities they chose, they simply would not be paid for selling a non-Merrill product (Wall Street Journal Aug. 11, 1989:C1).

In January 1990, Merrill Lynch announced that brokers would no longer be paid more for selling the firm's in-house mutual funds, but would be paid the same commission for all funds. At that time a company official said: "Basically, this whole idea of having the same payout for all products is a very professional approach" (Wall Street Journal Jan. 4, 1990:C1). This was a positive move for clients because it removed company pressure for brokers to put their own interests ahead of clients' needs. It also seems to indicate respect for the "professional approach" of brokers making decisions based on professional expertise unencumbered by company pressures. However, it would be naive to overlook the fact that the decision was made at a time when Wall Street firms were struggling to survive by cutting costs.

In spite of this change, Merrill Lynch continued its "broader strategy of moving toward paying brokers based on the total amount of client assets they gather, rather than on transactions" (Wall Street Journal Jan. 4, 1990:C1). Merrill's stated goal of paying brokers according to client assets is a move away from professional control of work based on fees for services rendered. It disadvantages small investors and the brokers who choose to serve them. Professional autonomy involves using professional expertise to meet client needs, and being paid a fee for these professional services. Merrill's plan would replace fees for services with company rewards for having a certain type of client with a certain size account. This is not necessarily an indication of deprofessionalization, since the firm continued to give brokers a choice of clients and type of work. However, there is certainly a strong possibility of deprofessionalization when the company overrides fees for services with compensation rules that are advantageous to the company but disregard professional fees for services to clients.

At Merrill Lynch, just as in the other two firms, content of work was basically controlled by the company. Brokers could make choices within the framework offered by Merrill Lynch, but did not control limitations in scope of work or expansion of jurisdictions. Merrill Lynch offered a wider variety of products and services than its competitors,

and continued to diversify its offerings during the period 1975 to 1990. Results of the content analysis show that 32 percent of Merrill Lynch articles mention expansion into jurisdictions of other professions, and 19 percent mention a full service competitive strategy. This diversification seems to have been generally favorable to stockbrokers in the firm, since it gave them a broad scope of work from which to choose.

Two examples indicate cases in which diversification was less favorable for the brokers. First, in the case of banking services, discussed earlier, the company was strongly identified with services that many brokers did not want as a part of their work, because they made no money from offering them. A second, and more potentially damaging example comes from Merrill Lynch's expansion into insurance products. Merrill linked the firm's success with insurance to its use of insurance specialists in its larger branches. These salaried in-house specialists work with the brokers, and have no clients of their own. Merrill reportedly showed interest in adding experts in other areas such as estate planning and taxation (Institutional Investor Jan. 1986:258). These plans, if carried out, could contribute to the deprofessionalization of stockbrokers in the firm by cutting them off from the advantages of diversification.

Effect of Scandals on Company Reputation

Articles concerning Merrill Lynch indicate moderate involvement in scandals. Thirty-four percent of Merrill cases mention some type of scandal, but only nine percent of these involved insider trading and none have to do with junk bond fraud. So while Merrill Lynch was involved in scandals, there was very little involvement in the high profile scandals that racked Wall Street in the period from 1975 to 1990.

Although the firm was not heavily involved in insider trading scandals, transactions in Merrill Lynch's Caracas, Venezuela office preceded the series of insider trading cases that started with Dennis Levine, and eventually connected to Michael Milken. After an internal investigation, Merrill Lynch officials alerted the SEC about suspicious transactions, information which led in turn to the discovery of Mr. Levine's insider trading scheme. The original trading irregularities investigated by Merrill also led to two former Merrill Lynch employees being charged with trading on inside information received indirectly from Dennis Levine (Wall Street Journal Aug.8, 1989:A2).

While avoiding the spotlight to some extent, Merrill was in the forefront of the "avalanche of bad publicity" surrounding single-premium deferred annuities issued by Baldwin-United Corporation. Merrill Lynch was the biggest seller of these annuities for which buyers made a single

payment, with taxes on the interest being deferred until money was withdrawn (Wall Street Journal April 18, 1983:18). In September 1983 Baldwin-United Corporation filed bankruptcy under Chapter Eleven, which allowed the company to operate while devising a plan to pay its debt. Baldwin's rehabilitation plan brought interest rates for annuity holders down two percentage points below the floor rate guaranteed by annuity contracts (Wall Street Journal Sept. 24, 1984:5), a situation that led to numerous lawsuits against brokerage firms that sold these annuities.

In January 1984, Merrill Lynch announced that it had set aside $88 million as partial reimbursement for its customers. "Merrill's decision to provide massive refunds so early in litigation may be unparalleled in securities-industry history" (Business Week Feb. 6, 1984:22). This move not only assisted Merrill clients, but also pressured other firms to offer reimbursements. Merrill's chief executive officer said: "We would like to emphasize that Merrill Lynch had no legal obligation under the policies to take these measures, but we acted to maintain the continued confidence of customers and potential customers" (Business Week Feb. 6, 1984:23.).

This "pioneering" move should have boosted the company's reputation, especially since months later two major brokerage firms continued to refuse to participate in a settlement plan involving a group of twelve brokerage

firms (Wall Street Journal Sept. 24, 1984:5). When negotiations faltered in this settlement plan, Merrill Lynch renewed its commitment to settle with its customers the 7.5 percent return guaranteed by annuity contracts. (Wall Street Journal Sept. 13, 1984:8).

Merrill Lynch's handling of the Baldwin situation indicates their willingness to make expeditious and substantial efforts to resolve problems. The firm not only attempted to solve problems, but also moved to reduce its risk in the wake of the Ivan Boesky insider trading case. Merrill announced that it would bring its arbitrage group "more under the control of its traditional stock trading operation" in an effort to try to figure out ways to "participate in a different environment." Wall Street Journal Feb. 4, 1987:3). Although Merrill's arbitrage operation comprised a very small part of its total operation, this new, lower risk arbitrage investment strategy was considered significant because it marked "one of the most sweeping assessments a major securities firm has made about the Boesky Scandal's impact on the stock market" (Wall Street Journal Feb. 4, 1987:3).

Merrill Lynch's overall moderate involvement in scandals and minimal involvement in widely publicized insider trading scandals are linked to efforts both to avoid risk and solve problems. This combination suggests less damage to the company's reputation than that experienced by

Drexel Burnham, which in turn would indicate less decline in client trust of stockbrokers at Merrill.

Effects of Organizational Responses on Deprofessionalization

Content analysis shows that Merrill Lynch responded to environmental changes by upholding its full service commitment while expanding into real estate, insurance, and banking services. About half of Merrill Lynch articles mentioned movement into new jurisdictions or the use of a full service competitive strategy. Merrill Lynch had long been recognized for its innovation and creation of new products and services. During this period Merrill used a full service competitive strategy in order to maintain leadership as "a financial supermarket capable of serving all its customers' needs" (Fortune Aug. 6, 1984:76).

As regulations separating banks and brokerage firms diminished, Merrill Lynch decisively stepped into banking services with its popular Cash Management Account. Merrill's diversification proved to be a strength to the company rather than a weakening factor. The firm made substantial moves into real estate and insurance services. Yet, it was noted that the further Merrill "branched away from its Wall Street roots, the stronger those roots have become" (Wall Street Journal Sept. 10, 1980:1).

As discussed earlier, the firm's diversification and commitment to full service were generally advantageous to

the maintenance of professional status of Merrill stockbrokers. The company's full service reputation served as a drawing card for clients and offered brokers a broad array of products and services from which to choose in serving their clients. However, there were some indications of company efforts to limit brokers' control of work through economic pressures and by the use of salaried specialists for some product areas.

The extent of Merrill Lynch's diversification was made possible by financial resources sufficient to follow numerous avenues, as well as compensate for failures. The company's very successful encroachment on banking turf began in 1975 with the Ready Assets Trust, which grew to be the largest of the popular money market funds offered by brokerage firms. Merrill Lynch's Cash Management Account, introduced in 1977, proved to be even more threatening to bankers. The Cash Management Account was said to be "a breakeven business at best", but gained the reputation of being the biggest and the best and it brought more than one million customers to the Merrill Lynch organization (Fortune Aug. 6, 1984:78).

Merrill's move into real estate proved to be much less promising than its offerings of banking services. Merrill Lynch viewed its entry into real estate as a way to broaden the firm's base by establishing relationships with clients "before they reached the prime investing years of middle

age" (Business Week Jan. 16, 1984:67). The assumption was that by helping consumers on what is usually their first big financial transaction, Merrill would have a foot in the door to sell insurance, stocks, and annuities later.

For the real estate venture to be successful for Merrill Lynch, the various real estate segments and other financial services needed to cooperate and generate business for each other. Getting these segments to cooperate proved to be difficult. After several years of erratic earnings and difficulties in integrating its real estate businesses into the securities operations, Merrill Lynch sold its real estate operations.

In other cases Merrill was able to replace unsuccessful programs or products. This was the case with their Personal Capital Planning Group, which was designed to provide customized planning in areas such as investments, taxes, and estates. This program was begun in 1976 as an early part of the firms's diversification drive into areas outside traditional brokerage business. After what Merrill Lynch management described as "only an anemic following", the program was replaced in 1982 by a scaled-down planning service known as Financial Pathfinder. The new service had a much lower fee and was targeted at a mass market (Wall Street Journal May 17, 1982:7).

Merrill Lynch's experience points out that with more financial resources there are more options for meeting

competitive pressure. However, the firm's extensive financial resources were greatly strained by several years of rapid expansion into diverse areas. This strain was exacerbated by severe market slumps in the late 1980's and by a system that required paying fees to brokers for the growing number of offerings at a time when competitors were using discount brokering and other low-cost distribution methods. As discussed previously, this economic strain led to a lower regard for stockbrokers as professionals, evidenced by company efforts to dilute the client-broker bond, compensation charges that increased company control, and use of salaried specialists for some product areas.

These efforts contributed to deprofessionalization, but were limited in scope. In spite of extensive diversification, the retail system of stockbrokers remained Merrill's greatest strength. Although the company attempted to weaken client-broker bonds, it is the broker, not the company, who typically commands client loyalty. While the firm attempted to exert control over brokers and cut costs through limited use of salaried specialists in some circumstances, Merrill executives knew from past experience that seemingly innocuous innovations could be sabotaged by brokers. One executive commented: "The typical broker sees any attempt to make a sale away from him as a potential threat to his relationship with his client, which he will defend to the death" (Business Week Jan. 16, 1984:62). This

suggests resistance to deprofessionalization by brokers at Merrill Lynch.

SUMMARY

As expected, Charles Schwab, Drexel Burnham, and Merrill Lynch not only responded in different ways to environmental changes and competitive pressures, but these differing organizational responses resulted in variation among firms in deprofessionalization of stockbrokers. Not only were organizational responses different, but responses varied in their effects on deprofessionalization. In some cases there was a direct effect on deprofessionalization, such as Charles Schwab's choice of a cost reduction strategy which led to a negation of professional status for stockbrokers in the firm. On the other hand, Drexel Burnham's choice of a special niche competitive strategy had an indirect effect on deprofessionalization. Choice of this strategy led to a detrimental pattern of resource allocation and was related to extensive involvement in scandals.

The choice of a cost reduction strategy had an overriding effect on deprofessionalization of stockbrokers in the Charles Schwab organization. The strategy led to employment of stockbrokers as salaried employees who were order-takers with no clients of their own. This makes deprofessionalization a non-issue in this firm, since the brokers did not have professional status. It also means

that brokers were out of the loop for any advantages gained by Schwab's diversification. In contrast to Schwab, Drexel Burnham offered its stockbrokers a great deal of control over their work. However, choice of the special market niche of junk bonds led to extensive involvement in scandals that, in turn, contributed to deprofessionalization by drastically diminishing client trust. This competitive strategy also led to resource allocation that favored the junk bond operation to the neglect of other parts of the organization, which in turn led to the sale of the retail brokerage operation, and eventually the company being bankrupt.

Effects on deprofessionalization were probably more mixed for brokers in the Merrill Lynch operation than in the other two companies. Merrill Lynch is larger, which indicates the likelihood of greater bureaucratic structure. Yet extensive financial resources gave the firm more options in dealing with competitive pressures. The firm's relatively low involvement in scandals protected company reputation and client trust. Merrill used a full service competitive strategy, and moved decisively into the jurisdictions of insurance, real estate, and banking services. This diversification seems to have been generally advantageous for Merrill brokers, since it provided a wide array of products and services to offer their clients.

In the latter part of the period the company attempted to limit brokers' autonomy through economic pressures, but these efforts were limited in scope. There were also efforts to weaken the client-broker bond by binding clients closer to the company, but client loyalty continued to be linked to brokers. Therefore stockbrokers at Merrill Lynch are more likely to retain autonomy than brokers in the other two firms. The company's moderate involvement in scandals and decisive action to solve problems also suggest higher levels of client trust for Merrill Lynch brokers. The strong position created by the firm's dependence on the retail brokerage operation and by client loyalty to brokers, gave Merrill Lynch stockbrokers some power in resisting changes that would be detrimental to their professional status.

CHAPTER 6

CONCLUSIONS

The review of literature in Chapter Two indicates a number of changes over time in sociological theory and research regarding the area of professions. Sociological investigation began by looking at the structure of professions as seen in traits evident in professions, but absent in other occupations (e.g. Greenwood 1957; Goode 1957, 1960). An ideal was developed identifying the free and autonomous professional with specialized knowledge and authority over clients. Professional development was traced, and this development was generally considered to have forward movement (e.g. Hughes 1958; Wilensky 1964).

However, by the 1970s sociologists began to question the image portrayed by earlier theory. There was a recognition of backward movement in professional development which was referred to as deprofessionalization (Haug 1973, 1975). Deprofessionalization is one of the primary issues addressed by professionalization literature in the past two decades. After recognizing that professions could lose status, sociologists began to investigate the process of deprofessionalization. As a result, a number of

environmental changes have been identified as factors contributing to deprofessionalization. Recognition of these environmental changes resulted in research that was no longer based on the assumption of professional development that inevitably moved in an upward spiral. Numerous social, economic, and political changes meant that the social environment was less likely to be a friendly environment for professional development.

As identification of deprofessionalization developed, there was also a growing interest among sociologists concerning the effect of organizational work on professionals. Scholars realized that the ideal of the free and autonomous professional no longer matched the reality of professional life for many professionals. In fact, it had never matched the reality of a number of professions, such as university professors, clergy, and military, who have always worked within organizations. By recognizing deprofessionalization and focusing on the growing prevalence of professionals within organizations, sociological study of professions moved toward a more realistic image of professionals and their work.

In this study I have brought together the elements of deprofessionalization and professional work in organizations. Much of the research on professionals working in organizations has focused on the inconsistency between bureaucratic structure and professional

characteristics (e.g. Hall 1968; Freidson 1984). However, as professionals continue to become increasingly identified with work in organizations, there is a need to explore other avenues concerning possible effects of organizational work on professionals. The effect of environmental changes on deprofessionalization is generally seen as a direct effect, but in this study I have argued that for professionals working in organizations, these environmental changes do not have a direct effect on deprofessionalization. Instead, the effects of these changes are mediated by organizational responses to the environment. Findings of the study confirm that firms do respond differently to the same environmental changes, resulting in variation in deprofessionalization among firms.

Specifically, this study investigated differences in organizational responses of three brokerage firms to the environmental changes of bank deregulation, changing technology, and rampant scandals in the securities industry during the period from 1975 through 1990.

Responses of each of the firms were ascertained by content analysis of 412 articles from the Wall Street Journal, Business Week, Fortune, and the Institutional Investor, all major sources of business and financial news. Tables 4.2, 4.3, 4.4 and 4.5 show that the data support the hypothesis that the brokerage firms studied each responded differently to environmental changes. Three very different

patterns of organizational responses were shown by the quantitative portion of the content analysis.

RESPONSES TO ENVIRONMENTAL CHANGES

Each firm chose a different competitive strategy in response to the intense competitive pressures resulting from banking deregulation. All three firms were connected to scandals, but each had a different level of involvement and activity. However, differences in responses to changes in technology were not as clear cut.

Bank Deregulation

Charles Schwab & Company adopted a low cost strategy made possible by the 1975 SEC ruling that ended fixed commission rates. The company was able to offer brokerage fees 30 to 70 percent below full service brokerage houses by limiting services and hiring brokers as salaried employees. Schwab brokers offered no investment advice and had no clients of their own since they were required to take client calls on a random basis.

Drexel Burnham & Company responded to increased competition by establishing a special market niche of junk bonds. Michael Milken, the "junk bond king", led Drexel into undisputed leadership in trading junk bonds. Articles concerning Drexel Burnham show virtually no interest in other competitive strategies or in diversification. Results of the content analysis indicate that the choice of the

special niche of junk bonds was the firm's singular response to increased competition resulting from banking deregulation.

Merrill Lynch & Company chose the competitive strategy of emphasizing full service, and responded to increased competition by extensive diversification. The firm moved aggressively into areas of banking services, real estate, and insurance products. It was an industry leader in offering new products and services to clients.

Technology

Merrill Lynch and Charles Schwab each had mentions of changes in technology in 18 percent of their cases. Most of the Merrill Lynch articles pertain to the failed International Marketnet venture, and are therefore irrelevant in determining deprofessionalization. Once Merrill Lynch articles pertaining to International Marketnet are disregarded, the remaining information technology articles deal primarily with Charles Schwab & Company.

Many of the Charles Schwab articles relate to technology designed to provide information and order entry capability for clients, and would thus be expected to contribute to deprofessionalization. However, this effect does not extend to Schwab stockbrokers since they do not have professional status.

Some information is available to individuals who are not Schwab clients through software available to the public.

Although information technology adopted by investors may have had an impact across the industry, there is no indication of widely available software having differing effects on deprofessionalization in the three firms in question. It seems that changes in technology may have resulted in deprofessionalization that was similar across firms. Overall, the articles concerning changes in technology were inconclusive and were not helpful in ascertaining differences in organizational responses to changes in technology by the three firms.

Scandals

Articles being analyzed mentioned scandals more frequently than any other category. Of the 262 cases involving scandals, 78 percent mention Drexel Burnham. Merrill Lynch and Charles Schwab not only had fewer reports of scandals, but also had mentions of company efforts to solve problems related to scandals.

Numerous reports of scandals may be due in part to the nature of the data. In some cases the number of mentions may indicate stories considered newsworthy, rather than the extent of impact on deprofessionalization. Therefore, the numerous cases concerning scandals may reflect perceived reader interest, but at the same time, differences among firms continue to be relevant regardless of the popularity of the subject.

EFFECTS OF ORGANIZATIONAL RESPONSES

Not only were there differences in organizational responses among the three firms, but the qualitative portion of the study indicates ways in which these differences influenced deprofessionalization. As expected, some organizational responses had a stronger impact on deprofessionalization than others. In all three organizations the competitive strategy chosen by the firm proved to be the strongest influence on deprofessionalization, but in each case the chosen strategy was linked to other organizational decisions. The impact on deprofessionalization cannot be ascertained by individual responses, but depends on the combination of choices made by a particular firm.

The low cost strategy adopted by Charles Schwab & Company involved reducing costs by cutting wages and limiting services offered to clients. However, this type of organization precludes two important aspects of professional work, the broker-client relationship and the use of professional knowledge and expertise to assist clients. Although Schwab made some movement into banking and insurance services and diversification of products and services, any positive effects of diversification for brokers were negated by limitations placed on brokers as a part of the firm's low cost strategy.

The competitive strategy of a special market niche seemed very successful for Drexel Burnham & Company for a number of years. Drexel became the industry leader in trading junk bonds. Initially, the financial success brought about by this market niche seemed advantageous for brokers in the firm. The company offered a good deal of autonomy to brokers, and their professional status was enhanced by the success of the firm.

However, when Drexel became heavily involved in scandals, company reputation took a nose dive, taking with it client trust in Drexel Burnham stockbrokers. As legal problems intensified, resources of the company were drawn away from other areas in order to bolster the junk bond operation. As a part of Drexel's settlement with the SEC, the firm agreed to closer supervision of its operations. This meant that all Drexel stockbrokers lost some of their autonomy. The final blow to stockbrokers in the company came when Drexel sold the retail brokerage portion of the firm in a last-ditch effort to salvage the junk bond operation. Drexel Burnham's choice of competitive strategy, and the ensuing involvement in scandals, resulted in loss of client trust and restrictions on autonomy for brokers in the firm and ultimately to bankruptcy for the company.

Merrill Lynch & Company chose a full service strategy carried out through decisive moves into new areas and extensive diversification. In contrast to Charles Schwab,

advantages of diversification in the Merrill Lynch organization seem to have been passed on to brokers in the firm. This was brought about by some combination of willingness by the company to include brokers and insistence by the brokers that they share these advantages. The data suggest that Merrill Lynch brokers had a stronger position in the firm than brokers in the other two companies, evidenced by their resistance to deprofessionalization. Merrill Lynch seems to have offered a fair amount of autonomy to its brokers, who in turn resisted attempts to restrict that autonomy.

DEPROFESSIONALIZATION

Deprofessionalization is a movement toward the nonprofessional end of the profession/nonprofessional continuum. The results of this study show that this movement is erratic, and that it has complex causal paths, rather than being driven by direct causal relationships. Strategic organizational choices made in response to a changing environment can accelerate or decelerate deprofessionalization for professionals within an organization.

At best, professionals are generally viewed as powerful and autonomous. At worst, they are seen as being subject to both the positive and negative effects of environmental changes affecting their area of work. However, the reality

is that many professionals are in organizational settings where they have virtually no protection from corporate decisions. These decisions can have adverse effects upon their professional life, or on the other hand, may bring profession enhancing results to the professional practitioner.

In the past deprofessionalization has been approached and investigated using the assumption that environmental changes have direct effects on deprofessionalization. While a variety of environmental changes have been linked to increased deprofessionalization, failure to consider mediating factors, such as organizational responses to these changes, oversimplifies deprofessionalization, resulting in limited understanding of the process.

SUGGESTIONS FOR FUTURE RESEARCH

This study points out the mediating effects organizational responses have on deprofessionalization of stockbrokers within three firms. It also suggests the possibility of incorporating the sociological study of professions into the strategic choice model (Kochan, Katz, and McKersie 1986, 1991). This may play a part in bringing sociological theory more in line with the reality of professional work, because it addresses the work of those in various levels of an organization in a way not usually seen in sociological literature concerning professions. At the

same time it may broaden understanding concerning the effects strategic decisions have on all levels of an organization, including professionals. One of the key issues I see coming out of this study is the realization of the complexity of the deprofessionalization process. If the study of professions and professional work is going to be useful, there is a need for the recognition and exploration of this complexity, and the strategic choice model seems to offer a promising avenue for this exploration.

This study points to the need for further investigation of organizational response as a mediating factor in the relationship between environmental changes and the status of professionals. Findings of this study have implications beyond the securities industry to the extent that professionals in other areas of work are subject to similar patterns of organizational response to environmental changes. In the past two decades numerous areas of work have been affected by increased competition. At the same time, professionals have been increasingly employed by organizations. These two factors emphasize the importance of studying the effects of organizational decisions on professionals in other areas of work.

Findings of this study suggest that professionals within a company are affected not only by specific organizational responses to environmental change, but also by other related organizational decisions. For example,

when a certain pattern of responses to competition result in decisions concerning allocation of resources, as seen in the case of Drexel Burnham, these decisions can have definite and perhaps devastating results for professionals within an organization. In fact, allocation of resources is a key issue for professionals working in organizations. It may prove fruitful to investigate how these decisions are made in various organizations, and who makes them. Professionals might be wise to seek ways to be a part of these decisions in order to protect their interests.

Studies of other professions concerning patterns of organizational decisions and their effects on deprofessionalization constitute an obvious first step in future research. However, this study not only suggests organizational patterns that increase or decrease the likelihood of deprofessionalization, but also elicits questions concerning factors that increase the possibility of resistance to deprofessionalization. For example, what combination of factors gave Merrill Lynch brokers the power to resist deprofessionalization to the extent suggested by these data? Is a similar combination of factors found in other professions that are faced with the need to resist deprofessionalization. For example, what determines success or failure in resisting deprofessionalization for clergy, many of whom are experiencing increased pressure from hierarchical dictates concerning Biblical interpretation and

liturgical practices? Also, could this type of question apply to university professors as universities experience continuing budget cuts, resulting in pressures that are passed on throughout the organization? Can professional freedom be protected, and under what conditions is this freedom likely to continue?

A number of answers to these questions come to mind. Although factors are likely to vary in importance in various professions, those with more education, a larger and more prestigious client base, and more experience are more likely to be able to resist deprofessionalization. Another factor that may be overlooked is the organizational structure of a particular firm. For example, Merrill Lynch's historical dependence on its retail brokerage unit gave Merrill Lynch brokers an increased ability to resist deprofessionalization. In addition to this overall advantage, within the firm the issues of client base and experience put some brokers in a more advantageous position for resistance to organizational pressures.

I believe the issues addressed in this study and the questions these issues pose contribute to the search for clearer and more realistic explanations of professions and professional work. Better understanding of the complexity of the deprofessionalization process is a crucial starting point in adequate explanations of changes in numerous professions. To gain an understanding of the complexity of

the deprofessionalization process requires an openness to new ways of looking at professions. It requires a willingness to borrow useful theories, to explore effects of organizational decisions, and to continue the move toward focusing on the work professionals do rather than on professional structure and development.

The issues of this study suggest several underlying questions concerning professions. First, we need to examine the traditional characteristics of professions. Perhaps in a time of better educated clientele the body of knowledge that identifies a profession has become less important. The deprofessionalization literature suggests this is the case. However, perhaps the extensive professional training and experience in applying the knowledge give a professional the ability to integrate various aspects of this knowledge in a way not generally possible for clients, even though they have access to a good deal of information. It may well be that the educational gap between professional and client is no longer as important as the ability through training and experience to put information together in ways that can prove advantageous to clients. This brings the question that needs to be explored. Is the general systematic knowledge that identifies professions still important, and if so, how has the meaning of this characteristic changed in a time of more knowledgeable clientele?

Another characteristic of professions is the norm of altruism, which indicates that professionals are identified by their altruism or community interest rather than by self interest. This characteristic seems far removed from professional practice as we generally see it. Should this characteristic be removed from our expectation of professionals? Is it a reasonable expectation for professionals working in organizations? These questions lead to the even broader question: Do these characteristics continue to be useful in identifying professions?

This is an important question to consider since lack of these characteristics is the basis for the identification of deprofessionalization. After two decades of describing professions as moving backward, as the terminology of deprofessionalization suggests, do we need a new definition of profession? Do we need to take a fresh look at the kind of work done by professionals, and how this work is carried out in an organizational setting? It may be that rather than simply moving backward, professions are branching out into new areas that were unknown and unexpected when the present definition of profession was developed.

APPENDIX A

CODING DESIGN FOR CONTENT ANALYSIS

PER	Newspaper or business periodical	
	01	Wall Street Journal
	02	Business Week
	03	Fortune
	04	Institutional Investor
MONTH	Month article published	
	01	January
	02	February
	03	March
	04	April
	05	May
	06	June
	07	July
	08	August
	09	September
	10	October
	11	November
	12	December
YEAR	Year article published	
	75	1975
	76	1976
	77	1977
	78	1978
	79	1979
	80	1980
	81	1981
	82	1982
	83	1983
	84	1984
	85	1985
	86	1986
	87	1987
	88	1988
	89	1989
	90	1990
FIRM	Firm referred to in article	
	01	Drexel Burnham
	02	Merrill Lynch
	03	Charles Schwab

JURISDICTIONAL COMPETITION:

COMPIN	Other professions into stockbroker jurisdiction
	01 Bankers
COMPNEW	Brokerage firms into new areas
	01 Banking services
	02 Insurance products
	03 Real estate
COMSTRAT	Competitive strategies
	01 Low cost
	02 Full service
	03 Special niche
	04 Mergers and acquisitions

TECHNOLOGY:

INFORM	Information services
	01 Adoption
PROG	Program trading
	01 Adoption
MARKET	Market services
	01 Adoption

SCANDALS:

SCANTYPE	Type of scandal firm involved in
	01 Insider trading
	02 Junk bond fraud
	03 Other type fraud
	04 Multiple types including insider trading
	05 Other multiple types
	06 Churning
SCANSOLV	Company response to scandal in terms of solution
	01 Company will solve

NO MENTION is represented by 00 in all categories

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