Michigan Law Review

Volume 32 | Issue 5

1934

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Recommended Citation
Laylin K. James, *THE SECURITIES ACT OF 1933*, 32 MICH. L. REV. 624 (1934).
Available at: https://repository.law.umich.edu/mlr/vol32/iss5/3

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THE SECURITIES ACT OF 1933*

Laylin K. James†

I

BACKGROUND OF THE SECURITIES ACT

IN 1907 a Pennsylvania superior court stated in one of its opinions that, " 'there is no reason why a man should not be a fool.' As a corollary to that saying, it may be added that there is no reason why a court should protect a fool against the result of his folly. No new feature of rapacity in the buyer is apparent in this instance [the purchase of property worth $5,000 prospectively for $500] to make him a worse offender against the law of fair dealing than an army of Shylocks who have preceded him. The patriarch Jacob bought a large landed estate from an improvident brother for the price of a frugal breakfast and the common parent when appealed to upheld the bargain. A 'catching bargain' much later in date than that between Jacob and Essau was passed upon in *Davidson v. Little*, 22 Pa. 245, when the owner of land worth $8,000 conveyed his interest for $200. The court held that the transaction was suggestive of fraud, but that the contract was binding if the vendor was of full age, of sound mind, acquainted with the necessary facts and subjected to no mental imprisonment."[1] The changes made in the applications of the fundamental common law doctrine during the twenty-six years that have since elapsed would make some of the old common law lawyers turn over in their graves. If one is to judge by the recently published statements on securities control many present-day lawyers, business men and bankers are preparing their minds for a communion of commiseration with those great stalwarts who have preceded them.

Beginning with the Kansas Securities Act, enacted in 1911, every State except Nevada has enacted some type of paternalistic legislation designed to protect investors in securities, protection, one might say "from the results of their folly." These statutes range from fairly complete control of the issue and sale such as exist under your Ohio act, to

* 48 Stat. 74; U. S. C. A. tit. 15, sec. 77a ff. (1933 Supp.).

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This article is a paper which the author delivered February 3, 1934, at the Law Institute sponsored by the Toledo Bar Association.—*Ed.*

[1] Singer's Estate, 217 Pa. 295 at 298, 66 Atl. 548 at 549 (1907).

fraud acts such as those of New York, New Jersey, Maryland and (surprising as it may seem) Delaware. Opinions on the effectiveness of the respective blue sky acts are as diverse as persons expressing them. That the effectiveness of their enforcement depends entirely upon the personnel of the officials in charge is conceded by all. Likewise there has been general agreement among the supporters of these acts that the federal mail frauds legislation needs to be supplemented to close certain interstate channels of communication to fraudulent securities vendors. Tangible expression of this latter agitation resulted in the introduction of several bills into Congress. The Taylor bill, introduced in 1919, incorporated a basic idea later embodied in the British Companies Act of 1929; that is, the requirement that promoters, directors and officers of corporations offering their stock to the public in interstate transactions should be required to file with a federal officer statements containing detailed information about their organization and prospects. This bill was never reported out by the committee to which it was sent. The Dennison bill, introduced in 1922, in substance sought to prevent the use of the mails and interstate communication to defeat the state blue sky laws; having passed the House, this bill died in the Senate Committee on the Judiciary. The Volstead bill was also still-born; it gave to the Attorney General powers to investigate alleged frauds in the sale of securities in interstate commerce and to issue stop orders. During the Seventy-Second Congress, which ended March 4, 1933, there were several bills introduced embodying various phases of the three bills just mentioned. And finally, the Seventy-Third Congress adopted the Securities Act of 1933 which became law on May 27, 1933.

Any appraisal of this federal legislation must visualize its setting. Beginning with the pseudo education accompanying the Liberty Loan drives, a large mass of the American public became security-investment conscious. The subsequent period of prosperity and inflation had several effects. It expanded savings with which this public blindly sought to achieve wealth and opulence overnight. Buyers turned increasingly to securities carrying higher yields in interest rates, such as debentures, foreign government and corporation bonds, construction bonds, stock equities ostensibly greater but necessarily greater risks, as evidenced by the complicated holding company pyramided stocks, stocks of new industrials such as radio companies, airplane manufacturing and transportation companies — each company assumed to be a potential Ford Motor Co. The smug took "flyers" and the uninitiated followed their own primitive instincts. And when I here refer to the public, I am

including the commercial bankers whose optimism caused them to be swept along with the speculative current.

Promoters and managements inspired and profited by this buying extravaganza. In their conscious or unconscious desire to get a portion of this easy capital they issued securities for overvalued properties, pyramided and complicated corporate structures, over-expanded, over-borrowed. Not only the promoters and managements accepted the golden opportunity, but the bankers likewise too frequently forgot their duty of counselors (not "Old Counselor"); they allowed the potential profits to color their advice, and to lessen their precautionary investigations; they marketed securities with little or no consideration of the productive or wasteful consequences; they reaped a harvest on the popularity of management and fixed trusts. We know they tolerated foreign graft in the competition for their own profits from marketing the foreign securities. Parenthetically, some of you probably know that "smoothing the palm" carried over into the purchase of commodities in our domestic markets. The spectacle of Chicago bankers literally thrusting upon Insull their accumulations of others' money is not an isolated page of the banker's responsibility. The Detroit River Bridge and Tunnel bonds, the 100 per cent financing of construction, show inexcusable failure to consider elementary business economics. Do not misunderstand me, I am not charging all these people with deliberate, malicious, illegal misconduct. The weaknesses of investors, promotors, management and bankers are not necessarily indicative of moral or economic turpitude. While one cannot measure accurately, I feel certain they are a result of the speculative mania of the inflationary era. On any logical basis the conduct to which I have referred compares favorably with that found in the less public affairs of the daily life of that period. Instance, if you will, the public apathy toward the Oil Scandals. The significance of reckless finance, however, with respect to the Securities Act of 1933 is not to be measured by its logical bearing but by its emotional effects. This is a matter to which I shall have occasion to revert later.

Another part of our picture contributing to the post-prosperity public clamor for protection was and is the clearly fraudulent security transaction. Estimates vary but there seems to be agreement in estimating minimum annual losses to American security buyers from patently fraudulent sales at approximately one billion dollars. The activities of George Graham Rice will illustrate. Born in the New York Ghetto, self educated while he served prison sentences, it is estimated that Rice

defrauded the public out of over $200,000,000. In him the tipster sheet had its first proponent. He operated the Iconoclast which had a circulation of hundreds of thousands. Selecting several leading securities, he established a deserved reputation for accurate forecast. Then he touted the stock of Idaho Copper, a corporation which he formed. He had its stock listed on the Boston Curb. Its property consisted of a water-filled, abandoned mine, the entrance to which was so overgrown that the federal investigators had difficulty locating it. His "boiler rooms" hummed with activity. One of his salesmen (a "dynamiter" in the parlance of the street) received over one and a half million dollars in commissions in five months. One of Rice's gestures was to publish a book entitled "My Adventures with Your Money," dedicated "To The American Damphool Speculator, surnamed the American Sucker, otherwise described herein as The Thinker, Who Thinks He Knows But Doesn't — Greetings! This book is for you! Read as you run and may you run as you read." The names of similar swindlers are legion: The Reverend (Fenwicke L.) Holmes, Esterday, Montgomery, Cox, yes, and the famous arctic explorer, Dr. Cook. These men and others like them sold stock "for the purpose of developing wildcat oil fields in distant states, imaginary mines in Peru, mythical railroads in Canada, for extracting gold from sea water, light from pomegranates and developing power from the rise and fall of the tides." "One original promotor mailed out circulars urging the purchase of stock in a spirit laboratory in which he expected to communicate with Steinmetz, consult him on new inventions and patent those he approved or suggested." [2] Without license or authority, these swindlers used such magnetic names for their fraudulent stocks as Ford of England, General Electric, and Montgomery Ward. Henry Ford's name was used in more than forty gyp organizations in New York City alone. It was Montgomery who duped Clarence Chamberlain into giving respectability to the Crescent Aircraft Corporation, and Lewis Yancy and Roger Williams into lending their names to Air Via Corporation. Partos, the Hungarian immigrant, among other practices, falsified balance sheets and earning statements. Among the fourteen corporations advertised by him and in which he sold stock, the following facts were discovered by the New York Bureau of Securities. "One was in receivership, one had been sold, the leasehold and rents of an-

[2] WASHBURN and DELONG, HIGH AND LOW FINANCIERS 15 (1932). The authors recount some interesting examples of striking fraudulent practices. The book reads like a modern Arabian Nights tale.

other had been assigned, two were no longer owned, one had been foreclosed and the remainder were returning no income." [3]

The fantastic schemes of such men were literally conceived one day, stock certificates rushed from the printers the next and sold to the gullible, rashly hopeful public before the week-end. They operated lavish financial speakeasies, crammed boiler rooms (Esterday's firm had more than fifty telephone salesmen in his boiler room; the telephone bills for one year exceeded $400,000). Bucket shops, installment plans, deposit plans for switching worthless for good securities, management trusts, pool operations, wash sales, high pressure salesmanship were all a part of their stock in trade. Only two weeks ago, Richard H. Brown and Charles H. McCarthy were convicted for mail frauds growing out of their part in the Manhattan Electrical Supply pool of 1930. Philbin's Atlas Tack pool is still fresh in your minds. Not only did this type of swindler rob widows and orphans on a grand scale, his victims included bankers, politicians, judges and business men, prominent in public affairs.

Between this crudest form of theft and swindling, and respectable investment and corporate business there is a twilight zone in which the practices are legal or illegal on the turn of one's mental state. You will recall Charles V. Bob and his meteoric rise in finance and antarctic geography. Engineer's Gold, which he backed, jumped overnight from seventy-five cents to $120 upon an insane engineer's report. Bob's part in the transaction may have been innocent. In any event his profits were a fortune. Likewise the securities in Metal and Mining Shares, Inc., an investment trust fostered by Bob, were siphoned off to his other companies. For his part in the transaction he was tried under eleven indictments, with a jury's disagreement as a result. Other practices were paying dividends out of capital, giving inaccurate earnings histories similar to Lord Kylsant's Royal Mail Steamship Line report, appraising rental properties for financing at prospective rents as if all the space were rented, using *pro forma* balance sheets where financing had not been completed and the probabilities of completion were an open gamble, giving valuable option warrants for small, if not questionable, consideration, paying sizeable bonuses to executive officers without complete disclosure to the shareholders, selling of bonds and preferred stocks with negligible common stock investments, and cumulative loading charges under management contracts.

Another factor in the general background of the Securities Act has

[3] WASHBURN AND DELONG, HIGH AND LOW FINANCIERS 174 (1932).

been the attack made upon the investment bankers and corporate managements by publicists. Louis D. Brandeis (now Justice) opened the way in 1914 by his book, "Other Peoples Money." Thorstein Veblen in his book, "Absentee Ownership and Business Enterprise," published in 1923, called attention to the separation of ownership and management in our corporation picture. William Z. Ripley, by his attack on some of the managements' and bankers' abuses of power, gave the impetus to much of the criticism of recent years.[4] Building upon Brandeis, Veblen and Ripley and particularly upon the fact investigations of Gardner C. Means, Adolf A. Berle has popularized and particularized these criticisms into a systematic philosophy which makes the development of the interrelations between the management and the bankers appear as a sinister and preconceived program to rob the public investors in corporate securities. These writers have performed a real service, however much they may have magnified the undesirable practices to justify their theories. For our purpose their work is important in that they have helped to create attitudes of mind which readily held the bankers and the management groups responsible for security losses.

In the setting for the enactment of the Securities Act the significance of the market crash in 1929 and the depression cannot be appraised properly without a consideration of the changes in the investment picture during the decade or more immediately prior thereto. It is estimated that from 1908 to 1929 the percentage of tangible wealth in the United States in the form of securities rose from 23 per cent to over 75 per cent.[5] From 1922 to 1929 the dollar total of new issues aggregated more than thirty-seven billion dollars. From 1900 to 1928 the number of stockholders of record increased from four million four hundred thousand to over eighteen million.[6] Allowing for duplications, the number increased almost five-fold. Almost overnight a large part of the public, whose savings had previously gone into institutions and indirectly into securities, were directly investing in securities.

According to a bulletin of the New York Stock Exchange the loss in paper values of listed securities as a result of the crash of 1929 and the continued depression was as follows: In January of 1931 bonds had a market value of over $47,000,000,000; by April of 1933 this value had shrunk to less than $31,000,000,000. Stocks in September

[4] W. Z. RIPLEY, MAIN STREET AND WALL STREET (1927).

[5] These figures are taken from G. W. Edwards, "Control of the Security Investment System," 12 HARV. BUS. REV. 1 (1933).

[6] BERLE AND MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY, c. 4 (1932).

1929 had a market value of over $89,000,000,000; in July 1932 a value less than $16,000,000,000. The holders of these securities also suffered from one or more of the following: shrinkage in land values, both rural and urban, and decreased income and production values. With a large group of investors swindled and defrauded by deliberate and systematic criminals, a larger group suffering tremendous paper and real losses from the market crash, a constant revelation of dubious corporate and banking practices, and an accusing finger pointed at the management and banking groups, it is not surprising that the investing public, looking for someone on whom to throw the blame, saddled responsibility for their security losses upon the groups mentioned.

Out of its despair and anger grew the tenth positive plank of the Democratic National Platform and thereafter the Securities Act of 1933. I recognize, of course, that other factors played a part in this enactment. It remains, however, not only that the psychological setting was perfect for the legislation but also that this setting will make particularly difficult amending the Act, if amendments are desirable.

II

PROVISIONS OF THE ACT

Essentially the Securities Act aims at two things — (1) that there shall be filed with the Federal Trade Commission a full, accurate and complete statement of all pertinent facts concerning issues of the securities; and (2) that instruments of transportation or communication in interstate commerce and the mails shall not be used directly or indirectly to effectuate fraudulent sales.[7] In the discussion of the Act I shall consider its provisions as follows: (1) securities and transactions to which the Act applies; (2) registration; (3) the prospectus; and (4) civil and criminal liabilities arising from false registration statements, prospectuses and communications.

1. *Securities and Transactions to Which the Act Applies — Exemptions*

"Security" is defined broadly in the Act to include "any note, stock, treasury stock, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement,

[7] The original bill, besides certain other features hereafter mentioned, gave the Federal Trade Commission authority to forbid the issuance of securities of any corporation in an "unsound condition" or "not based upon sound principles."

collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of interest in property, tangible or intangible, or, in general, any instrument commonly known as a security, or any certificate of interest or participation in, temporary or interim certificate for, receipt for, or warrant or right to subscribe to or purchase, any of the foregoing." With the exceptions of "certificate of . . . participation in any profit-sharing agreement" and "investment contract" this definition of itself probably is no broader than that contained in your Ohio Securities Act. The definition was lifted almost bodily from the proposed Uniform Sale of Securities Act adopted by the National Conference of Commissioners on Uniform State Laws in October, 1929.

Section 3 exempts the following from the definition of securities: those "sold or disposed of by the issuer or bona fide offered to the public" within 60 days after the enactment of the Act, that is between May 27, 1933, and July 26, 1933; United States, domestic States, and municipal securities or those guaranteed by the United States or domestic States or municipalities; securities issued or guaranteed by the Federal Reserve Bank, any national bank or state or territorially supervised bank; current notes, drafts, bills of exchange or bankers acceptances with maturities not exceeding 9 months; securities of non-profit organizations, such as religious, educational, benevolent, fraternal, charitable or reformatory, in which "no part of the net earnings inures to the benefit of any person, private stockholder or individual," securities of building and loan, homestead, savings and loan associations substantially all the business of which is confined to making loans to members and where the issuer takes no more than 3 per cent of the face value as fees; securities of farmer's co-operative associations; securities issued by "common carriers subject to the provisions of section 20a of the Interstate Commerce Act"; certificates issued by a receiver or trustee in bankruptcy with the court approval; insurance or endowment policies or annuity contracts or optional annuity contracts issued by a corporation which is subject to the supervision of certain designated public officers; and finally the Federal Trade Commission is empowered to exempt issues up to $100,000 if it finds enforcement of the Act in such cases not necessary in the public interest and for the protection of investors.

The Act fails to make certain fairly standard exemptions made by the state blue sky laws. This has been a fertile source of criticism of the Act by certain groups of issuers and their counsel. The state laws

have generally exempted securities listed on the New York, Chicago and Boston Stock Exchanges; some add the Chicago Board of Trade, and the New York and Boston Curb markets. The securities of a foreign government or securities guaranteed by a foreign government do not usually come within the state acts. And public utility securities supervised by public officers and securities guaranteed by railroads and public utilities are likewise usually exempt.

The theory underlying the federal Act justifies the refusal to allow such exemptions. The registration statement theoretically furnishes complete and accurate information which, also theoretically, will furnish purchasers of securities a basis for intelligent judgment upon which they will invest. Such information has as much significance in respect of any of the securities usually exempted as in respect to securities not exempt. To be sure, the theory of most of the usual exemptions is that some reasonable effort has been made to elicit such information. Exchanges and government officers who supervise railroads and public utilities may have secured such information but the investing public has no access to it. These exemptions are based upon the likelihood that the judgments of exchange and government officers will be a reasonable check upon the flotation of fraudulent securities. No one can challenge the important part played by the New York Stock Exchange in protecting investors by careful examination of listing applications, by insisting upon quarterly reports to shareholders, and by exercising careful scrutiny of current practices. You all remember how effectively the Exchange ended Allied Chemical's practice of carrying millions of dollars of treasury stock as an asset. Some of you probably have experienced the rigid listing requirements. So, too, the other exchanges may have exerted a desirable influence in keeping doubtful securities off the list or in supervising corporate practices. Likewise utilities commissions and the Interstate Commerce Commission have exerted a desirable restraining influence in supervising securities issues by those corporations under their respective jurisdictions. We all know, however, that the effectiveness of stock exchange and utilities commission supervision depends too largely upon personnel to insure a uniformly high degree of effectiveness. But granted such uniform effectiveness, the Securities Act is founded upon disclosure plus liabilities in those cases where there is an untrue statement of a material fact or an omission to state a material fact required to be stated in the registration statement or necessary to make the statements therein not misleading. There is no reason why utilities or corporations, whose

securities are listed on specified exchanges, or those other parties enumerated in the Securities Act should be preferred over other corporations or other parties in not being required to state the truth about their respective enterprises or held liable for material misstatements or omissions. If there is any argument to justify making the usual exceptions, it is one of convenience. Those who criticize the Act have not clearly recognized the limitations of their arguments. That it may be more expeditious in marketing securities to relieve such corporations from preparing and filing the registration statement, and the Trade Commission from examining and filing such statements, is far from conclusive. If the theory of the Act is sound, the failure to make these exemptions is also sound. Moreover, many securities of such commonly exempted classes have been marketed where the filing of a registration statement might well have been a preventative. I doubt whether Insull's corporate hierarchy could have marketed all its conglomeration of stocks and bonds if it had been required to comply with a law similar to the Securities Act. A cursory perusal of the proceedings of the National Association of Securities Commissioners will give plenty of illustrations of failure of exchanges and utilities commissions.

At the risk of anticipating, somewhat, subsequent developments in my talk I want to point to one other absent exemption. Failure to exempt foreign government securities raises at least two problems. New financing in the United States may and probably will be reduced to a minimum. The information required in the registration statement to be filed in foreign government issues will cause many such issuers to turn to other nations for financing. The waiting period after filing the registration statement provided in the Act, not to mention the time necessarily required to prepare the statement, will make firm commitments by American bankers either impossible or much more costly to the foreign borrower. Nor will the foreign representatives be anxious to incur possible liabilities under the civil liability sections. I also think some of our neighbors to the South and some of our European friends will even be reluctant to tell just who gets consideration from the issue. Bearing in mind that foreign bankers will not be handicapped in this manner, to the extent that this financing can be managed abroad, the American market will lose this financing. If we were starting from scratch, perhaps the present prejudice against lending to foreign countries might well insist upon prohibitory conditions. But we must recognize that much of the $7,000,000,000 of foreign securities sold in the United States from 1920 to 1930 will have to be refunded. The Act

will handicap our own investors to the extent that the foreign issuers are unable to refund here. To pay in goods or to refund in foreign countries and buy dollars to pay American security holders raise problems not answerable in terms of prejudice. I make no profession of experience with problems of foreign exchange or trade. It takes no great amount of intelligence, however, to sense problems here which cut to the heart of complicated and increasingly difficult international relations. I commend to your attention in this connection the article of John Foster Dulles in the October 1933 issue of Foreign Affairs entitled, "The Securities Act and Foreign Lending."

Section 3, sub-paragraph (1) exempts "any security which, prior to or within sixty days after the enactment of this title, has been sold or disposed of by the issuer or bona fide offered to the public, but this exemption shall not apply to any new offering of any such security by an issuer or underwriter subsequent to such sixty days." By the "but" clause the exemption does not apply "to any new offering of any such security by an issuer or underwriter made after such sixty day period." What do the expressions "bona fide offered to the public" and "new offering of any such security" mean? "Bona fide offered to the public" is not an expression of art. It has no clearly defined meaning though each of us probably has some notion of its meaning. Nor has this expression been clarified by decision under the state blue sky laws. The nearest approach to decisions on the point is found in the Alabama court's construction of that State's Securities Act.[8] These decisions on method point to an offering by advertisement, circulars or prospectus which is made to the public generally. Similarly, it is impossible to determine accurately the meaning of "new offering of any such security." Does this mean a new public offering or any offering less limited? Probably the courts will construe this as meaning a new public offering.

As to the number of persons to whom it is offered and how far their number determines whether the offering is "public," attention is called to Section 4 which specifies exempt transactions. Some have believed that offering stock to shareholders or other already existing security holders of the issuing corporation is not a public offering. Paragraph (3) of Section 4 exempts transactions which involve existing security holders exclusively, subject to the limitations stated therein. Normal

[8] Raynard v. State, 19 Ala. App. 281, 96 So. 723 (1923); Robertson v. Business Boosters' Country Club, 210 Ala. 460, 98 So. 272 (1923); 212 Ala. 621, 103 So. 576 (1925); Gillespie v. Long, 212 Ala. 34, 101 So. 651 (1924). See also Bates v. Firestone, 19 Ohio App. 243 (1924); In re Leach, 215 Cal. 536, 12 Pac. (2d) 3 (1932).

construction would seem to indicate that, if it were necessary to state this exemption in the act, such transaction would otherwise have been within public offering. That this was contemplated by Congress is indicated by the statement of the Managers on the part of the House at page 25 of the Conference report which is as follows: "Sales of stock to stockholders become subject to the act unless the stockholders are so small in number that the sale to them does not constitute a public offering." The Trade Commission has so construed the Act in their release of December 29, 1933.[9] The Commission also holds in the same release that an offering to employees of sufficient number (2450 employees in the case before it) was a public offering.

It is interesting in this connection to see that one of the keenest students of the Securities Act does not agree with the Trade Commission. Mr. Arthur Dean, of the firm of Sullivan & Cromwell, suggested in July 1933 that, while the courts and the Trade Commission may decide differently, the following are not public offerings as that term is generally understood:[10]

(1) The sale by a corporation of limited amounts of treasury stock to selected individuals;

(2) The issuance by a corporation of its own stock to its employees;

(3) The exercise of a subscription or conversion privilege by a holder of a subscription warrant or convertible security now outstanding;

(4) The issuance of certificates of deposit to certain security holders by a reorganization committee.

On the questions of method of offering and the number and status of persons to whom the offer is made in determining "public offering" the federal and state courts will likely follow the views here expressed on the method of offering and the status of those to whom the offer is made. How many persons will have to be involved can only be answered by court decisions.

Another problem of construction of Section 3, sub-paragraph (1), may arise where an underwriter has made a bona fide public offering of 100,000 shares of the corporation's stock on July 26, 1933. He can continue this offer until the shares are sold. After July 26, 1933, an additional block of the same stock is offered by the issuer without filing a registration statement. Section 5 makes it unlawful for any person directly or indirectly to use "any means or instruments of transporta-

[9] New York Times, December 30, 1933, p. 8.
[10] FORTUNE, August 1933, pp. 50 ff.

tion or communication in interstate commerce or of the mails to sell or offer to buy" securities as to which a registration statement is not in effect, or "to carry or cause to be carried through the mails or interstate commerce, by any means or instruments or transportation any such securities for the purpose of sale or for delivery after sale." If the underwriter of the block offered on July 26, 1933, should attempt to support the market and should have thereby innocently acquired some of the second issue shares and offered them innocently within the meaning of Section 5, he may have violated the Act. So, too, a broker may have violated the Act who solicits orders in transactions involving the shares but which without his knowledge include some of the second issue. If a registration statement has been filed, sales of the securities would still raise difficult problems in determining which class is being offered, and the dealer can only protect himself by delivering a prospectus as to every security offered.

I call to your attention one further illustration in connection with the exception in Section 3, sub-paragraph (1). A corporation has issued convertible securities or employees options prior to July 26, 1933, the privileges of which are not immediately exercisable. The issue of securities under the conversion privilege or upon the exercise of the options after July 26, 1933, may be a public offering and is certainly a sale under Section 2, paragraph (3). In which case the issuer cannot legally issue or deliver the security in interstate commerce or through the mails without filing a registration statement and without delivering a prospectus, nor can the holder of the convertibles or the options mandamus the issuer.

The difficulties may be obviated by the issuer's registering all of its securities of the class which it proposed to issue after July 26, 1933, whether issued before or after July 26, 1933. This, however, requires a broad construction of the registration statement by the Trade Commission, a construction by no means certain to be made.[11] The suggested possible confusion and potential liability of dealers, brokers and issuers will be eliminated thereby. To leave the dealers, brokers and holders of convertibles and options to the caprice of the issuer is undesirable and unfair.

Paragraph (a) (2) of Section 3 exempts securities issued or guaranteed "by any national bank, or by any banking institution organized under the laws of any State or Territory, the business of which is substantially confined to banking and is supervised by the State or terri-

[11] See last sentence of Sec. 6 (a).

torial banking commission or similar official." The Glass-Steagall Act [12] will eliminate the security affiliates problem one year from June 16, 1933, as to "member banks," but any securities of, or guaranteed by national banks or banking institutions, which are "member banks," issued after July 26, 1933, and prior to June 16, 1934, where there are security affiliates not yet disposed of will raise the uncertain question of what is meant by "business substantially confined to banking." Similarly, the problem will be present with trust companies which do both banking and other types of business. Paragraph (a) (5) of Section 3 raises the same problem with building and loan associations, homestead associations, savings and loan associations. I do not raise this problem as a criticism of the Act — rather, I merely point to it as a warning.

The Trade Commission in the exercise of power conferred upon it under paragraph (b) of Section 3 has already specified certain exemptions.[13] Essentially these are: (1) notes and bonds comprising an issue in the aggregate not exceeding $15,000 secured by a first mortgage or deed of trust on real estate or long-term lease on which there is a dwelling for not more than four families, one of which must be that of the issuer; (2) securities not exceeding in the aggregate $100,000 with specific limitations as to other issues, denominations and par or stated values; (3) securities issued in exchange the aggregate amount of which do not exceed $100,000, subject to certain stated limitations.

Unless a registration statement is in effect as to a security, Section 5 makes it unlawful for any person, directly or indirectly, (1) to use any of the "means or instruments of transportation or communication in interstate commerce or . . . the mails to sell or offer to buy such security through the use or medium of any prospectus or otherwise," (2) "to carry or cause to be carried through the mails or in interstate commerce, by any means or instruments of transportation, any such security for the purpose of sale or for delivery after sale"; (3) to carry or transmit in interstate channels or through the mails a prospectus which fails to comply with the Act; (4) to carry or cause to be carried through the mails or in interstate commerce for the purpose of sale or for delivery after sale any such security unless accompanied by a prospectus complying with the Act. Paragraph (c) of Section 5 provides that the foregoing provisions "relating to the use of the mails [and note that the reference is to the mails and not to other channels of interstate

[12] U. S. C. A. tit. 12, sec. 336 (1933 Supp.); 48 Stat. 165 (1933).
[13] Rules and Regulations Adopted November 1, 1933.

communication or commerce] shall not apply to the sale of any security where the issue of which it is a part is sold only to persons resident within a single State or Territory, where the issuer of such securities is a person resident and doing business within, or, if a corporation, incorporated by and doing business within, such State or Territory." Under the exception just stated it is a nice question whether an offer of securities within a single State can be made by newspaper advertisement. The Trade Commission has ruled that such advertisement in a newspaper which is sold beyond the domestic State, with the following hedge-clause, is not within the exception: "This offer is open only to residents of the State of X." The Commission stated that "the use of any means or instruments of transportation or communication in interstate commerce, whether it were mail, express, freight, telephone or telegraph, would require registration. This would be true, even though the specific conditions of Section 5(c) were met — that is, even though the issue were sold entirely to residents of the State in which the issuer was incorporated and doing business. The clause suggested, therefore, seems insufficient, but it would seem possible to frame a clause which would have the effect of nullifying the advertisement as an offer as soon as it entered interstate commerce." [14]

Section 4 provides that certain security transactions shall be legal without a registration statement having been filed. These include, (1) "transactions by any person other than an issuer, underwriter or dealer . . ." (a dealer is defined in Section 2 to mean "any person who engages either for all or part of his time, directly or indirectly, as agent, broker or principal, in the business of offering, buying, selling, or otherwise dealing or trading in securities issued by another person"); (2) those "by an issuer not with or through an underwriter and not involving any public offering"; (3) those "by a dealer, . . . except transactions within one year after the last date upon which the security was bona fide offered to the public by the issuer or by or through an underwriter" and except "as to securities constituting the whole or a part of an unsold allotment to or subscription by such dealer as a participant in the distribution of such securities by the issuer or by or through an underwriter"; (4) "brokers' transactions, executed upon customers' orders on any exchange or in the open or counter market, but not the solicitation of such orders"; (5) "the issuance of a security of a person exchanged by it with its existing security holders exclusively, where no commission or other remuneration is paid or given directly or

[14] New York Times, December 30, 1933, p. 8.

indirectly in connection with such exchange"; (6) "the issuance of securities to the existing security holders or other existing creditors of a corporation in the process of a bona fide reorganization of such corporation under the supervision of any court, either in exchange for the securities of such security holders or claims of such creditors or partly for cash and partly in exchange for the securities or claims of such security holders or creditors." It will be noted from the foregoing exemptions under Section 4 that transactions under Section 5 are materially limited thereby, that ostensibly the exemptions in Section 4 include all transactions by any person other than an issuer, underwriter or dealer, and that in addition certain transactions by issuers and dealers are exempt.

Section 4 in several respects is ambiguous. It is questionable whether all of its restrictions are necessary for the protection of investors. (1) Reading the section along with Section 5 a dealer who does not participate in the distribution of a security cannot make sales or purchases, through the mails or the use of the instruments of interstate commerce, of an issue of securities without furnishing a prospectus. When we remember that a dealer is defined to mean "any person who engages either for all or part of his time, directly or indirectly, as agent, broker, or principal, in the business of offering, buying, selling, or otherwise dealing or trading in securities issued by another person" it is obvious that investors will be handicapped by not being able to use their own dealers. (2) It will be extremely difficult to determine what is "one year after the last date upon which the security was bona fide offered to the public." When sales by those marketing the securities initially continue indefinitely and without definite public information thereof, it seems this exemption may be meaningless in practice. (3) Brokers, who are not dealers, may execute orders on any exchange but cannot solicit such orders. Does "solicitation" refer to brokers who solicit as principal only or as agents for others? (4) Securities may be exchanged by a "person" with its existing security holders exclusively "where no commission or other remuneration is paid or given directly or indirectly in connection with such exchange." No such exchange can be made where any considerable amount of securities are outstanding without incurring some expense such as depositories' fees, transfer agents and registrar fees, counsel fees, advertising and the like. The exemption probably means, and the Chief of the Securities Division of the Trade Commission has informally stated, that no commission or remuneration shall be paid to any dealer or other third party to induce

the security holder to make the exchange.[15] Nevertheless, until there are decisions a lawyer will find it difficult to advise clients when such exchanges can safely be made without filing a registration statement. (5) The reorganization exemption is much narrower than would appear at first glance. The exemption covers the "issuance of securities to the existing security holders or other existing creditors of a corporation in the process of a bona fide reorganization of such corporation under the supervision of any court" but must involve an exchange or partly an exchange and partly cash. You will note that the exemption applies only to corporations. Thus, unincorporated associations and business trusts are not included. It is limited to reorganizations and does not cover readjustments or compositions. The preliminary stages of a reorganization are not covered. Thus, committees which secure deposits and issue certificates of deposit must file registration statements. The committees, when they have prepared a plan of reorganization, find the plan a prospectus under the definition of that term and they must therefore comply with the provisions of the Act relating to prospectus before the plan can be distributed (Secs. 2 (10), 5, 10). Also when the securities are ready for delivery they too require a registration statement in practice, for not all of them will be exchanged under the reorganization plan and those left over must be sold to raise the cash requirements to pay off security holders who elect to take cash and to finance the new corporation. The question of liability of committees in this connection will be apparent when we consider civil liability generally.

We have thus far considered what securities and transactions come within the provisions of the Act. We turn now to the actual issue of securities under the Act.

2. *Registration*

A corporation desires to sell an issue of first mortgage bonds in the aggregate principal amount of $10,000,000. Normally it will go to its bankers and make preliminary arrangements (Sec. 2 (3)) whereby the bankers either underwrite the offering which the corporation desires to sell to the public or purchase the bonds outright from the corporation and resell them to the public. At this point the Act requires the filing of a registration statement[16] signed by the issuer, "its principal

[15] Proceedings of National Association of Securities Commissioners, 1933, pp. 107, 108.

[16] Secs 6 and 7.

executive officer or officers, its principal financial officer, its comptroller or principal accounting officer, and the majority of its board of directors." The statement must contain the detailed information, and be accompanied by the documents specified in Schedule A of the Act, and must contain such other information and be accompanied by such other documents as the Trade Commission may by rules or regulations require as being necessary or appropriate in the public interest or for the protection of investors. "If any accountant, engineer, or appraiser, or other person whose profession gives authority to a statement made by him, is named as having prepared or certified any part of the registration statement, or is named as having prepared or certified a report or valuation for use in connection with the registration statement, the written consent of such person shall be filed with the registration statement." However, the Commission is permitted to dispense with the written consent of persons named in the registration statement as having prepared reports or valuations used in connection with the registration statement but not named as having prepared the same for use in connection with the registration statement.[17] All signatures on the registration statement are presumptively affixed thereon with proper authority.[18]

If the statement is on its face incomplete or inaccurate in any material respect, the Trade Commission may issue an order prior to the date on which the statement becomes effective (which is the twentieth day after its filing) refusing to permit the statement to become effective.[19] No one will suppose the Commission's determination will be challenged in the courts. It scarcely needs saying that whatever market there might have been would be destroyed by the suit. If an amendment is filed prior to the effective date, the registration statement will be deemed to have been filed at the time the amendment is filed, thus postponing the effective date.[20] If, however, the amendment is filed with the consent of the Commission prior to the effective date of the registration statement or filed pursuant to an order of the Commission, such amendment shall be treated as a part of the registration statement.[21] An amendment filed after the effective date shall become effective on such date as the Commission determines, having due regard to the public interest and the protection of investors.[22] The Commission may at any time after fifteen days notice issue a stop order suspending the effectiveness of the registration statement if it appears

[17] Sec. 7. [18] Sec. 6 (a). [19] Sec. 8 (b). [20] Sec. 8 (a).
[21] Sec. 8 (a). [22] Sec. 8 (c).

to the Commission that the registration statement includes any untrue statement of a material fact or omits to state any material fact required to be stated therein, or necessary to make the statement therein not misleading.[23]

Schedule A, which specifies the information to be contained in the registration statement, contains thirty-two paragraphs. I intend to call attention only to certain of these paragraphs. Some balance sheets may but need not be certified by an independent public or certified accountant;[24] profit and loss statements must be so certified. But if the balance sheet submitted is as of a date not more than 90 days prior to filing and is not certified by an independent public or certified accountant, then a balance sheet as of a date not more than one year prior to filing, certified by an independent public or certified accountant must be filed.[25] If the proceeds or any part of the proceeds of the security to be issued are to be applied to the purchase of any business, the balance sheet of the business to be acquired must be certified by an independent public or certified accountant.[26] A copy of the opinion or opinions of counsel in respect of the legality of the issue must be filed.[27] The following information concerning security ownership of the issuer must be included: (1) "the names and addresses of all persons, if any, owning of record or beneficially, if known, more than 10 per centum of any class of stock of the issuer, or more than 10 per centum in the aggregate of the outstanding stock of the issuer as of a date within 20 days prior to the filing of the registration statement";[28] (2) the amounts of securities of the issuer held by directors; the chief executive, financial and accounting officers, promoters (if business was formed within two years prior to filing), underwriters and those persons who own more than 10 per centum of any class of stock or in the aggregate of the issuer as of a date within 20 days prior to the filing of the statement and if possible as of one year prior thereto, and the amounts of securities for which such persons have indicated their intention to subscribe;[29] and (3) "a statement of the securities, if any, covered by options outstanding or to be created in connection with the security to be offered, together with the names and addresses of all persons, if any, to be allotted more than 10 per centum in the aggregate of such options."[30]

The following required information relates to the directors, officers and large stockholders of the issuer: (1) "the remuneration, paid or

[23] Sec. 8 (d).
[24] Schedule A, (25), (26).
[25] Schedule A, (25).
[26] Schedule A, (27).
[27] Schedule A, (29).
[28] Schedule A, (6).
[29] Schedule A, (7).
[30] Schedule A, (10).

estimated to be paid, by the issuer or its predecessor, directly or indirectly, during the past year and ensuing year to (a) the directors . . . and (b) its officers and other persons, naming them whenever such remuneration exceeded $25,000 during any such year";[31] (2) "full particulars of the nature and extent of the interest, if any, of every director, principal executive officer, and of every stockholder holding more than 10 per centum of any class of stock or more than 10 per centum in the aggregate of the stock of the issuer, in any property acquired, not in the ordinary course of business of the issuer, within two years preceding the filing of the statement or proposed to be acquired at such date";[32] (3) and "any management contract or contracts providing for special bonuses or profit-sharing arrangements, and every material patent or contract for a material patent right, and every contract by or with a public utility company or an affiliate thereof, providing for the giving or receiving of technical or financial advice or service (if such contract may involve a charge to any party thereto at a rate in excess of $2,500 per year in cash or securities or any thing else of value), shall be deemed a material contract." [33]

Specific information is required concerning the issue to be sold as follows: (1) "the specific purposes in detail and the approximate amounts to be devoted to such purposes, so far as determinable, for which the security to be offered is to supply funds, and if the funds are to be raised in part from other sources, the amounts thereof and the sources thereof";[34] (2) "the estimated net proceeds to be derived from the security to be offered";[35] (3) "the price at which it is proposed that the security shall be offered to the public or the method by which such price is computed and any variation therefrom at which any portion of such security is proposed to be offered to any persons or classes of persons, other than the underwriters, naming them or specifying the class";[36] (4) "all commissions or discounts paid or to be paid, directly or indirectly, by the issuer to the underwriters in respect of the sale of the security to be offered. Commissions shall include all cash, securities, contracts or anything else of value, paid, to be set aside, disposed of, or understandings with or for the benefit of any other persons in which any underwriter is interested, made, in connection with the sale of such security. A commission paid or to be paid in connection with the sale of such security by a person in which the issuer has an interest or which is controlled or directed by, or under common

[31] Schedule A, (14).
[32] Schedule A, (22).
[33] Schedule A, (24).
[34] Schedule A, (13).
[35] Schedule A, (15).
[36] Schedule A, (16).

control with the issuer shall be deemed to have been paid by the issuer. Where any such commission is paid, the amount of such commission paid to each underwriter shall be stated";[37] (5) "the amount or estimated amounts, itemized in reasonable detail, of expenses, other than commissions, . . . incurred or borne by or for the account of the issuer in connection with the sale of the security to be offered or properly chargeable thereto, including legal, engineering, certification, authentication, and other charges";[38] (6) "the net proceeds derived from any security sold by the issuer during the two years preceding the filing of the registration statement, the price at which such security was offered to the public, and the names of the principal underwriters of such security";[39] (7) "any amount paid within two years preceding the filing of the registration statement or intended to be paid to any promoter and the consideration for any such payment";[40] (8) "the names and addresses of the vendors and the purchase price of any property, or good will, acquired or to be acquired, not in the ordinary course of business, which is to be defrayed in whole or in part from the proceeds of the security to be offered, the amount of any commission payable to any person in connection with such acquisition, and the name or names of such person or persons, together with any expense incurred or to be incurred in connection with such acquisition, including the cost of borrowing money to finance such acquisition";[41] (9) "full particulars of the nature and the extent of the interest, if any, of every director, principal executive officer, and of every stockholder holding more than 10 per centum of any class of stock or more than 10 per centum in the aggregate of the stock of the issuer, in any property acquired, not in the ordinary course of business of the issuer, within two years preceding the filing of the registration statement or proposed to be acquired at such date." [42]

And I must mention two further requirements of Schedule A. (1) The issuer must furnish the dates and parties to, "and the general effect concisely stated of every material contract made, not in the ordinary course of business, which contract is to be executed in whole or in part at or after the filing of the registration statement or which contract has been made not more than two years before such filing." [43] (2) Copies of all such contracts, of all underwriting agreements, all agreements giving commissions or discounts, material management contracts and

[37] Schedule A, (17).
[38] Schedule A, (18).
[39] Schedule A, (19).
[40] Schedule A, (20).
[41] Schedule A, (21).
[42] Schedule A, (22).
[43] Schedule A, (24).

profit-sharing arrangements, material contracts for a material patent right; of all contracts with a public utility company or an affiliate thereof for giving or receiving of technical or financial advice or service and copies of the underlying agreements or indentures affecting any stock, bonds or debentures offered or to be offered.[44]

Without considering other requirements of Schedule A, certain observations readily suggest themselves as regards the requisite information already mentioned. Our corporation will not be anxious to disclose all this information even assuming all of it is pertinent. Where there are options, profit-sharing contracts, bonuses, promoters profits, directors and officers favors, expenses coming within the definition of commission, or management contracts, there will be more than reluctance to disclose. Likewise the underwriting details require coercion to get them out in the open. The magnitude of information required will be an expense. (The commission's form is 26 legal-size pages.) It makes possible honest mistakes which may be construed as untrue statements of material facts; it makes possible omissions to state material facts which are required to make the statements not misleading. The task of preparation in the case of a sizeable corporation is one of no small import. Where the Act requires a "concise" statement in the case of "material contracts" [45] or itemizing "in reasonable detail" the expenses of sale,[46] misstatements or omissions are easily possible.

One's first inclination is to wonder why some matters are omitted; for example, the availability and cost of energy supply, the growth of the business, local competition or regulatory conditions, raw material supply, the labor situation, methods of merchandizing and credit terms. Slight consideration brings a realization that many of these factors omitted are matters of opinion rather than fact, that many of them are bound to be speculative in character and therefore of little value.

The registration statement as set out in Schedule A has some decided merits. Those who have raised the loudest outcry against the voluminous and searching character of the registration statement have insisted upon one of the theories of the Act. They insist the investor cannot form an intelligent judgment from the statement because of its size, and I think they are right if one thinks of the great bulk of investors as they are. The act unquestionably contemplates the ideally intelligent investor. One can only speculate on the number of individual investors who can read intelligently a registration statement; the percentage, I hazard a guess, can be stated by one digit. The number who

[44] Schedule A, (28), (30). [45] Schedule A, (24). [46] Schedule A, (18).

will take the trouble to get these statements will be even less, for the cost of 20 to 25 cents per page[47] will discourage some of the few who might understand them. This alone is not an answer, however. Any of you, who have had clients in a position where inside information on secret profits, bonuses, management fees, loans to officers, bankers' commissions and the like have had to be published, know the salutary effect thereof. Some of you may know of the directors who have paid from their own resources loans which they authorized from their corporation's funds to cover margin accounts of executives, paid only when publicity was threatened. If this smacks of distrust of corporate management and investment banking practice, so be it. Our statute books are full of laws which make more onerous the path of the honest because some are dishonest. That the Securities Act in this respect will have a decided influence to curb the over greedy in the corporate management and investment banking field, I feel certain. Would Dillon, Read, for example, have taken the common stock equity in one of their management trusts for a negligible consideration and asked the public to furnish the real capital through preferred stock had they faced publicity before the offer to the public? [48] Mr. Wiggins did not long insist upon his pension after the Congressional Committee gave it publicity. Indeed, I am inclined to think the reputable managements and bankers will welcome the publicity. As I understand it, the Commission has shown itself very sympathetic with the issuers, and personally I would like to see the existing registration statement given a full fair trial; I would expect the helpful co-operation of the Commission in accepting statements in the best condition possible with hedge clauses and also amendments. I shall revert later to some of the problems of the registration statement, in considering the liabilities of the persons concerned.

3. *The Prospectus*

Having filed the registration statement, and the twenty-day period having elapsed so that it becomes effective, our corporation and the underwriters are still unable to make deliveries of the securities through the mails or in interstate commerce for the purpose of sale or for delivery after sale unless the same are accompanied or preceded by a prospectus which meets the requirements of the Act.[49] By Section 10 the

[47] Sec. 6 (d); Rules and Regulations, Art. 9 (effective July 6, 1933).

[48] HEARINGS BEFORE THE COMMITTEE ON BANKING AND CURRENCY, United States Senate, Seventy-Third Congress, 2d Sess., pp. 2117 ff. (1933).

[49] Sec. 5.

prospectus must contain practically all that the registration statement does except the copies of counsel's opinions, agreements, contracts, underlying agreements or indentures and the organization papers of the issuer. The Commission is authorized to approve eliminations from the prospectus of any information required in the registration statement as not being necessary or appropriate in the public interest, or for the protection of investors. For the same reasons the Commission may also require additional information to be inserted in the prospectus. A prospectus cannot be used more than thirteen months after the effective date of the registration statement unless the information therein shall be as of a date not more than twelve months prior to such use.[50] Whether this latter provision requires a new registration or an amendment involving new liabilities is uncertain. If it does, dealers who cannot compel a new registration will suffer a real and undeserved hardship.

It is important to bear in mind that "prospectus" under the Act does not necessarily mean what we have in the past understood by it. By Section 2, paragraph (10), "the term 'prospectus' means any prospectus, notice, circular, advertisement, letter, or communication, written or by radio, which offers any security for sale; except that (a) a communication shall not be deemed a prospectus if it is proved that prior to such communication a written prospectus meeting the requirements of section 10 was received, by the person to whom the communication was made, from the person making such communication or his principal, and (b) a notice, circular, advertisement, letter or communication in respect of a security shall not be deemed to be a prospectus if it states from whom a written prospectus meeting the requirement of section 10 may be obtained and, in addition, does no more than identify the security, state the price thereof, and state by whom orders will be executed."

From these combined sections it is patent that issuers and underwriters cannot proceed along the old lines in marketing securities. Unless they have furnished a prospectus complying with Section 10 they cannot safely communicate with prospective purchasers of securities in offering securities for sale. This is subject only to the exception that they may use notices, circulars, advertisements, letters or communications if therein it is stated from whom a written prospectus may be obtained and such notices, circulars, advertisement letters or com-

[50] Sec. 10 (b) (1).

munications do no more than identify the security, state the price thereof and state by whom orders will be executed.

The comments already made as regards the registration statement are all pertinent to the prospectus. One point made should be emphasized here. By article 16 of the Rules and Regulations of the Trade Commission it is provided that "The information set forth in the prospectus, including financial statements, except as to the latest balance sheet and the profit and loss statement for the latest fiscal year, may be expressed in a condensed or summarized form . . . provided that such condensation and rearrangement shall not omit any item of information which may be material or may be necessary in order that the other statements contained in such prospectus shall not be misleading. . . . " You men know the possibilities of honest, innocent error when one attempts to condense or summarize. The urge to condense in this instance will be great. The expense of preparing the prospectus will magnify this urge. If condensation is indulged in, hedge clauses ought to be inserted with regularity. Arthur Dean advises the use of the following:[51]

> "This sets forth certain information which we think will be of interest to you, but it does not purport to give a full and complete analysis. Additional information will be furnished on request. No representations other than those contained in this document are authorized to be made in our behalf."

I am not satisfied that this hedge clause will eliminate liability if the condensation omits a material fact. But when one considers that the Commission does generally authorize condensation, that those securing the prospectus are given the opportunity to get additional information, that the statements as made are given in good faith (though a chancellor or jury will have to determine this), the chances are more than even that liability will not result if some material fact is omitted.

4. *Civil and Criminal Liabilities for False Registration, Statements, Prospectuses, and Communications*

Let us assume that our corporation has prepared and filed its registration statement, that its prospectus has been given to the purchasers, and that either or both contain untrue statements of a material fact or omit to state a material fact necessary in order to make the statements

[51] Arthur Dean, "Economic and Legal Aspects of the Federal Securities Act of 1933," PROC. NAT. ASS'N OF SECURITIES COMMISSIONERS, 1933, p. 160 at 170.

therein not misleading. What liabilities may result? Sections 11, 12, 15 and 24 purport to answer.

Sections 11 and 15 contain the civil liability provisions dealing with registration statements. Those made liable are, (1) "every person who signed the registration statement" (you will recall that those required to sign are the principal executive officer or officers, the principal financial officer, the comptroller or principal accounting officer and the majority of the board of directors of the issuer); (2) "every person who was a director of, . . . or partner in, the issuer at the time of filing the part of the registration statement with respect to which his liability is asserted"; (3) "every person who, with his consent, is named in the registration statement as being or about to become a director . . . or parner" of the issuer; (4) "every accountant, engineer, or appraiser, or any person whose profession gives authority to a statement made by him, who has with his consent been named as having prepared or certified any part of the registration statement, or as having prepared or certified any report or valuation which is used in connection with the registration statement with respect to the statement in such registration statement, report, or valuation, which purports to have been prepared or certified by him"; (5) "every underwriter with respect to such security"[52] (While we have used the term "underwriter" before, its definition here becomes of vital consequence. "Underwriter" by Section 2, paragraph 11 is defined to mean "any person who has purchased from an issuer with a view to, or sells for an issuer in connection with, the distribution of any security, or participates or has a direct or indirect participation in any such undertaking, or participates or has a participation in the direct or indirect underwriting of any such undertaking; but such term shall not include a person whose interest is limited to a commission from an underwriter or dealer not in excess of the usual and customary distributors' or sellers' commissions."); and (6) "every person who, by or through stock ownership, agency, or otherwise, or who, pursuant to or in connection with an agreement or understanding with one or more other persons by or through stock ownership, agency, or otherwise, controls" any of the persons named above.[53]

The most striking feature of the Act is the scope of this liability. Each and every person who may be sued is made liable jointly and severally, with one exception,[54] for the whole amount of the issue. He may be held either in an action to rescind or for damages to every per-

[52] Sec. 11 (a).

[53] Sec. 15.

[54] Sec. 11 (f).

son buying a registered security entitled to rely upon the registration statement whether in fact such buyer relied upon it or not.

Liability may be avoided by all such persons except the issuer and those who, by or through stock ownership, agency, or otherwise, control the issuer. But any such person who seeks to escape liability must be able to show that he resigned before the effective date of the registration statement and notified the Commission, or that if the part of the registration statement involved became effective without his knowledge, he so resigned and so notified the Commission and gave public notice,[55] or that after reasonable investigation and in the exercise of reasonable care he believed the statement made to be true and that there was no omission to state a material fact.[56] In determining what constitutes reasonable investigation and reasonable ground of belief, the standard of reasonableness shall be that required of a person occupying a fiduciary relationship.[57] Except those exclusively guilty of fraudulent misrepresentations, persons liable are given a right of contribution "as in cases of contract from any person who, if sued separately, would have been liable to make the same payment." [58]

No other part of the Securities Act has produced so much controversy as Sections 11, 12 and 15. Both those favoring the Act and those criticizing it have spent much of their ink on inconclusive arguments, frequently merely resorting to arguments *ad hominem*. But some of the contentions merit our consideration.

Many object to abandoning the old common law doctrine of "let the buyer beware" for that adopted, which is, "let the seller beware" — and the Act adds sufficient sanction to enforce the change. Historically the common law theory developed in a period when both the buyer and the seller knew or were in a position to know fairly well about the subject matter of the sale. The buyer usually had before him a tangible object that contained within itself specific information necessary to judge its quality. And today the situation as to tangibles is not entirely different. True, the refinements of tangible property brought about by our mechanical age makes it much more difficult for the buyer to know of defects. He can, however, at no great effort secure the advice of one who knows about the tangible property. The buyer of securities has no such possibilities. He must of necessity rely upon what the original seller tells either to him or to the public generally. And if he cannot appraise such information himself he can ask the local

[55] Sec. 11 (b) (1) (2). [56] Sec. 11 (b) (3). [57] Sec. 11 (c).
[58] Sec. 11 (f).

business leaders (yes, I mean the local investment and commercial bankers!) who in turn must rely upon the same original source, though they may have available other information on which to judge. In a simple capital structure this judgment may not be inaccurate intrinsically, though the many matters of opinion and chance involved may make their judgment no more than a guess. In any case the seller can be expected to follow the practice in other fields and make the best prospectus he can for the security. And just consider the complexity of some of our modern capital structures. Mr. Owen Young is reported to have said of the capital structure of the Insull system, "I think it is impossible for anyone to get an accurate picture of the Insull set-up and I remember the feeling of helplessness that came over me when I began in February, 1931, to examine the structure." Who can appraise fairly the securities of the Associated Gas & Electric? Moody's 1931 Manual lists eighteen issues of bonds and debentures of top holding company, ten classes of preferred and common stock, a class of allotment certificates and several classes of rights. In its system are fifty-four companies, a large number of which have several issues of bonds and stocks. When we realize that within the last ten years $60,000,000,000[59] of securities have been marketed, we cannot ignore the helplessness of the vast majority of investors. This vast sum ought not to be risked blindly; there is no adequate social or economic reason why it should be risked without the possibilities of fairly complete information, the accuracy of which shall be guaranteed by civil liability penalties. The law ought to attempt to put the sellers and buyers on something like equal terms.

The other side might be stated by paraphrasing the late Roberts Walker's diatribe against some of our neighboring courts' attitude toward the director's fiduciary duty to stockholders:[60]

> The issuer's and banker's "superior knowledge" counts as omniscience. The investor's knowledge, wisdom or obligation of candor is as naught. The Congress which enacted the Securities Act seemed to cherish the mental picture of shrewd, sharp, scheming issuers and bankers craftily trading with inexperienced, female, infant, defective investors. In a word, the kind of investor for whom the law should guarantee bank deposits, prohibit cigarettes, control reading matter and provide curfews.

[59] Means, G. C., "Protecting the Buyers of Securities: A New Approach," New York Times, April 9, 1933, Sec. 8, p. 3.

[60] Walker, "The Duty of Disclosure by a Director Purchasing Stock from His Stockholders," 32 YALE L. J. 637 at 640 (1923).

But Section 11 does not stop with putting the buyer in the position to know. It enforces civil liability even though the buyer did not rely upon the registration statement, provided that statement contained "an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading." There is some justification for this enactment. Certainly at the time when the issue is sold and for some period thereafter, the information in the registration statement will have a real bearing upon the market. It will affect the market through investment bankers, others with technical staffs and individual investors with especially intelligent marketing background. Later other factors will enter to affect the market price and the registration statement will have increasingly less effect. The Act makes no allowance for this fact; the maximum period of limitation of actions to enforce civil liability is ten years after the security is offered to the public.[61]

Along with the provision freeing the purchaser from the necessity of proving reliance we must consider an equally significant provision of Section 11. Paragraphs (e) and (g) provide: "The suit authorized under subsection (a) may be either (1) to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security or (2) for damages if the person suing no longer owns the security." "In no case shall the amount recoverable under this section exceed the price at which the security was offered to the public." In itself rescission for material misrepresentation, even though the present worth of the subject matter of the sale has depreciated for other reasons, is nothing new in our law. But it must be remembered that suits may be brought for rescission against many who are not in the position of vendors, so that the analogy to precedents is not complete. Rescission can be had against parties many of whom never received any consideration from the sale of the security. And again it must be remembered that under the Act a showing of reliance is not necessary, even though the suit is begun just short of the ten-year statute of limitations period. The extent of the damages offers a chance for possible inequity and gives those potentially liable great cause for reluctance in inviting such suits. Nothing in the Act of itself indicates that the damages recoverable need result from the misstatement or omission. Some argue that reasonable construction should limit damages to those flowing from the misstatement. But "reasonable" in such an argument expresses a personal reaction.

[61] Sec. 13.

When the issue comes before the courts they will have to face these considerations. The basis of the wrong is misstatement or omissions of *material* facts. Material to what? They must be material to the registration as a true and accurate picture of the merits of the security insofar as the statement discloses it. But the materiality over this possible ten-year period goes to but one point of time, and that is the time at which the registration statement was filed. Does the elimination of proof of reliance by implication remove the necessity of tying up the damages claimed to the misstatement or omission? Allowing damages not flowing from the wrong done is contrary to the common law. Can the court say the language of Section 11 is sufficiently explicit to justify the conclusion that Congress intended to eliminate the causal relation between the wrong done and the loss suffered? Section 12, subparagraph (1) makes the seller liable who sells when a registration statement has not been filed or a prospectus delivered as provided in Section 5. The damage suit in such a case is virtually meaningless unless the liability is absolute. One may say this part of Section 12 is not inconsistent with the necessity of proving causation under Section 11. The remedy of rescission under Section 12 is present and also the plaintiff purchaser probably would have no means of proving a causal relation. In any event the courts will have to harmonize the two sections. While my own belief is that the courts will be inclined to hold a causal relation necessary, this result is by no means certain and the problem is intensely real to those who may be subjected to liability and to their counsel. Until there are judicial constructions, this possibility will have a tremendous dampening effect on financing. We have only to recall October 1929 to realize the possibilities of such potential liability.

Section 11 would permit those acquiring the securities to sue every underwriter. You will recall that "underwriter" includes the primary underwriter who purchases from the issuer or sells for the issuer, and also those who participate or have a direct or indirect participation in such undertaking, and those who participate or have a participation in the direct or indirect underwriting.[62] The only ones excepted are those whose interest is limited to a commission from an underwriter or dealer not in excess of the usual and customary distributor's or seller's commission. Theoretically, therefore, the participant in Toledo who obligates himself in a subsyndicate arrangement to take $200,000 of bonds in a $10,000,000 issue may have rescission suits on $10,000,000 of bonds and/or suits for damages by those who have been holders of all out-

[62] Sec. 2 (11).

standing bonds. In these suits the damages may be the difference between the issue price and the then market price though the lower market price may be caused by factors having nothing to do with the misstatement or omission. But practically it is inconceivable that all such suits will be brought against one minor participant. Everyone knows those bonds will be scattered all over the United States and probably in other countries, and that a New York or Denver purchaser is unlikely to bring suit against the Toledo participant on bonds marketed by a New York syndicate. Moreover, many of the sales will be entirely intra-state and will not involve the use of the mails or of any instruments of interstate commerce. Whatever Congress intended or said, it has no jurisdiction over a purely intra-state sale. Also paragraph (f) of Section 11 gives to each person sued a right of contribution against all persons who, if sued separately by the holder of the security, would have been liable. It is inconceivable that the primary underwriters and subunderwriters in the event of suits against our Toledo banker will sit idly by and risk an adverse decision. Then the Toledo participant may also be able to sustain the burden of proof that he exercised reasonable care and so was not to blame for not discovering the untrue or omitted statement, a burden which will not normally be as difficult for him as for the officers and directors and the primary underwriter. And finally, in the event of rescission suits the participant will have the bonds; they are not apt to be worthless though the immediate market may well be depressed, and thereafter offers to sell within the Act will have to be preceded by pointing out the untrue or omitted statement.

It should be conceded also that to limit the investor to suits against his vendor may not give him an adequate remedy for at least two reasons: his vendor may not be an underwriter or participant, and if he purchases on a stock exchange he may have difficulty in proving who the actual underwriter or participant was who sold the security into the investment chain. The Act therefore very properly allows wider remedies than this; it should and does allow remedies against the issuer, its officers, directors and controlling interests. But the difficulties of an investor, limited to remedies against his vendor, furnish no adequate excuse for all of the many and unlimited liabilities of the Act. In not frankly admitting the investor's need for remedies besides those against his vendor, the critics of the Act are at fault. They are also to blame for not admitting the practical considerations which lessen the probability or alleviate the burden of the minor participant's liability. On the

other hand, the supporters of the Act as it stands are equally at fault in trying to use these considerations as a complete answer to unfounded fears. No lawyer can advise a banking client to take the risks thus entailed without pointing them out. Few reputable bankers are likely to want to assume such risks where the possibilities of errors are great, and obviously the larger and the older the issuing corporation the greater the possibility of error. Only if the profit on such a participation were somewhat commensurate with the risk, could the banker be expected to go ahead.[63]

Many other arguments are made against the liability provisions of Section 11 upon which I shall only briefly comment. (1) Not a few persons decry the shifting of the burden of proof to the defendants to establish the exercise of reasonable care. But the old legal formula of the plaintiff's burden has nothing sacred about it. I see no reason why those who have possession of the facts should not be compelled to sustain them.[64] (2) Others object that those liable should have the duty to investigate or form beliefs and exercise care which the law fixes upon fiduciaries as provided in Section 11. The cases exact only reasonable care from trustees, the most important class of recognized fiduciaries. The American Law Institute Restatement of the Law of Trusts accepts this standard of care for trustees.[65] (3) The critics and the supporters of the liability provisions of the Act both refer to the English Companies Act of 1929 to sustain their positions. The real issue in respect to the Securities Act is its intrinsic provisions and not whether it is modeled upon, follows or goes beyond the Companies Act. (4) The provision for liability for omission to state a material fact required to be stated in the registration statement or necessary to make the statements therein not misleading is not entitled to all the argument made about it. This provision is analogous to that in the English criminal statutes under which Lord Kylsant was convicted.[66]

There are other possibilities of civil liability under the Act to which I shall refer. Section 12, paragraph (2), provides liability predicated upon the prospectus. A sale of a security, whether the security be ex-

[63] Section 22 makes jurisdiction on questions arising under the Act concurrent in all state and territorial courts as well as the federal courts. This means that the business man's fears and counsel's advice must be predicated for years to come upon the uncertainties of diverse decisions.

[64] See, for example, Industrial Research Corp. v. General Motors Corp., (D. C. W. D. Ohio 1928) 29 F. (2d) 623 at 626.

[65] RESTATEMENT OF THE LAW OF TRUSTS, Tentative Draft No. 2 (1931), sec. 169.

[66] Rex v. Kylsant, 23 Cr. App. R. 83, [1932] 1 K. B. 442.

empted or not, "by the use of any means of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of circumstances under which they were made, not misleading," subjects the seller to civil liability. Note that this liability runs from the seller to his immediate vendor. The remedies for this liability are the same as those found in Section 11, that is, rescission and damages. The seller can defend by sustaining the burden of proof that he did not know and in the exercise of reasonable care, could not have known of such untruth or omission. Here again reliance, causation, misrepresentation and damages are irrelevant. This section, as I have already indicated, fixed an actual liability upon a seller who sells when no registration statement has been filed or when a prospectus does not precede or accompany the delivery of the security as provided in Section 5.

By Section 17 of the Act fraudulent transactions in securities sales are made illegal where any means or instrument of transportation, or communication in interstate commerce or the mails are used. These provisions are designed to cover direct and indirect fraudulent inducements and tipster sheets. No securities are exempt from the section. While the language in the paragraph covering tipster sheets and so-called investment counsel is ambiguous, some such provision has long been needed to supplement mail frauds legislation by giving federal law enforcement officers control over boiler room operators and fraudulent investment counsel. No civil liabilities are stated in the section nor are any penalties stated therein. The common law civil liabilities are probably not enlarged by the section though rescission may be made available because of the declared illegality. Willful violations unquestionably are subject to the criminal penalties provided in Section 24. Under Section 20 the Trade Commission can investigate and enjoin such violations.

III

SOME POSSIBLE EFFECTS ON INVESTORS AND BUSINESS

Our discussion of liabilities leads us to a consideration of probable effects which the Act will have upon business. No legislation can protect a fool against the results of his folly. Nor can it educate the public with savings to invest intelligently, cure its avarice and greed, or eliminate stupidity and cupidity. The Rices, Montgomerys, et al. will

never be eliminated by statutes nor will their future victims fail to respond to the lurid glamorous pictures of wealth overnight. We must also keep constantly in mind that the Act is but one step in any effective scheme to control finance in the social interest. Telling the truth about securities at the time of issue cannot protect investors against questionable management practices, against manipulations of corporate finance permitted under some of our corporation statutes, or against manipulations of stock exchange transactions.

Probably the business man will have to accept the Act as it is. At the present time there is little public indication at least that either the Administration or the Trade Commission favors amendments. A newspaper report of January 18, 1934, indicated that a conference between the President and Attorney General Cummings, Secretary Morganthau, Senator Dill, Representative Rayburn, Commissioners Matthews and Landis and the general counsel to Secretary Morganthau resulted in no plan to change the Act in its general features, but the suggestion was made that there might be some smoothing out of the Act's administrative features. Just what, if any, amendments will be made no outsider knows. When one glimpses the background of the Act as I have partially painted it, when one contemplates the increasing evidence being elicited by congressional investigators of borderline, if not fraudulent, practices of bankers, both commercial and investment, and of business men, I am frank to say I do not anticipate any very fundamental amendments.[67]

Changes in business practices are apt to follow. It needs no saying that bankers will have to exercise much greater care in telling investors what the bankers themselves want to know, or in seeing that such information is in the registration statement and prospectus; that they will have to give all information known to them which in any material way tends to qualify information in the statement or prospectus. One well-known New York firm advises its clients particularly on balance sheets and earnings statements as follows:[68]

"(a) If net earnings are given before depreciation, be sure to so state and state the amount of depreciation. Earnings should

[67] Since this paper was delivered, an Interdepartmental Committee has reported suggested changes to the President. See WALL STREET JOURNAL, Feb. 7, 1934, p. 12, where it is said, "While members of the committee refused to indicate the nature of the report, it is known that several committee members favor modifications of some of the more drastic liability provisions of the act."

[68] PROC. OF NAT. SECURITIES COMMISSIONERS, 1933, p. 160 at 170.

preferably be given on an 'overall' and not an 'after-times' basis or should preferably be stated both ways.

"(b) Any losses charged directly to surplus and not taken out of earnings should be stated, if known.

"(c) If there is any money in closed banks the amounts should be stated.

"(d) Any important qualification as to receivables or merchandise should be stated.

"(e) If there is any important item on the balance sheet, the heading of which may give rise to erroneous impression, it should be amplified.

"(f) Wherever possible, the balance sheet should indicate whether assets are carried at cost or market or appraised value and if market is above or below cost, it should wherever possible be stated. There are exceptions to this in case of fixed investments.

"(g) If a corporate or a consolidated balance sheet or earnings statement would in your opinion give an erroneous impression, a breakdown should be given.

"(h) That they should try to understand the make-up of each item on the balance sheet and to avoid items such as 'Government and other Securities.' "

We would all agree, I think, that such methods are not only wholesome now but would have been just as wholesome before the enactment of the Securities Act.

The Trade Commission may through its rules and regulations in connection with the registration statement aid in standardizing accounting methods, balance sheets, income and surplus statements. But experts, such as accountants, who have established reputations for honesty and integrity are not likely to assume readily the risks under the Act. Consequently their work may well fall into the hands of the least desirable of their profession.

A desirable change may, I believe, be effected in the personnel of our boards of directors. Window dressing will be less common. The English system of managing directors seems to be forecast with its concomitant salaries for directors' services commensurate with the duties and obligations imposed upon them. With the greater possibilities of risk and the possibility that the Trade Commission will look askance at complicated corporate structures, simplification therein may also follow.

The immediate effect of the Act upon financing has been the subject of acrimonious argument. The critics of the Act point to the present depression and the necessity to secure a return of the flow of capital

into industry; to the fact that within the next year over one billion dollars of refunding must be done. They insist that this is being held up by the Act;[69] that one reason why this flow has continued to be dammed up is fear on the part of the bankers and also the officers, directors and the interests controlling the issuers. That there is apprehension no one doubts. The other side points out that there is no private railroad financing though railroads are exempt from the Act; that the municipals market has been inactive; that the speculative industries which hold the popular fancy — distilleries and gold mines — are securing capital. They maintain that credit shrinkage is mainly due to the loss of faith in credit-worthiness, to the drying up of institutional investments because of the financial difficulties of insurance companies, savings banks, trust companies, building and loan associations, and to the gun-shy attitude of investors with funds, who are themselves on strike against the bankers.[70] No one can accurately weigh the arguments. The truth is that only time can decide the weight of these arguments.

In the meantime, there is not the slightest doubt that reluctance to hazard the risks is real. Mr. Grace in issuing the annual report to Bethlehem shareholders only a few days ago is reported to have said,

> "I do not believe we will be on a permanent foundation for recovery until business is in a position to raise private funds for its capital needs. The Securities Act of 1933 is playing a part in the lack of private financing. I know of numerous cases where money would be spent for capital purposes but for the restrictions imposed by the act. Of course other factors of uncertainty are playing a part in retarding the use of private capital. We hear much today about 'priming the pump'. What we would like to know is when the opportunity is to arise for industry to finance itself in the normal manner." [71]

[69] Arthur Dean, "Economic and Legal Aspects of the Federal Securities Act of 1933," PROC. NAT. ASS'N OF SECURITIES COMMISSIONERS, 1933, p. 160; W. M. Wherry, "The New Federal Securities Act," 12 PUB. UTIL. FORT. 123 (1933); G. A. Brownell, "The Federal Securities Act of 1933," BARRONS, July 10, 1933, p. 3; G. A. Brownell, "How Can the Securities Act Be Made Workable?" BARRONS, November 6, 1933, p. 3; A. A. Ballantine, "Amending the Federal Securities Act," 20 A. B. A. J. 85 (1934).

[70] B. B. Bane, "The Securities Act of 1933," PROC. NAT. ASS'N OF SECURITIES COMMISSIONERS, 1933, p. 94; B. Flexner, "The Fight on the Securities Act," ATLANTIC MONTHLY, February, 1934, p. 232. Since delivering this paper the first utility issue has been registered under the Act, a $15,000,000 bond issue of American Water Works and Electric Company, Inc., for refunding purposes. See New York Times, February 9, 1934, p. 27.

[71] New York Times, January 26, 1934, p. 25.

Mr. Grace's view undoubtedly represents that of a considerable group of industrial executive leaders. They not only fear possible liability as executives and directors but are keenly aware that Section 15 makes every person, who controls the issuer, jointly and severally liable — and that there are no defenses for this latter group, not even those defenses afforded to the directors and officers of the issuer. A small issue house in a neighboring city after the Securities Act became law examined a group of its old circulars and prospectuses. It had put out seventeen issues only five of which were carried into default by the depression. It found that ten of these were capable of being held to contain untrue statements of material facts or material omissions. It concluded that the issue business had better be handled by others. I am informed by a disinterested observer that this house had an excellent reputation for integrity and conservativeness, that it employed equally reputable and conservative accountants and engineers. One of the leading firms of accountants in the United States has refused to participate in the preparation of registration statements except for old clients. Lloyd's have notified accountants that their liability policies will not cover the Securities Act liabilities. Mr. George O. May, of the firm of Price, Waterhouse & Co., in an address before the Illinois Society of Certified Public Accountants in December of last year, made the following observations:

> "It is clear that the accountant may incur liability under the Act without being guilty of either moral culpability or recklessness, if a court holds that either (a) facts within his knowledge were presented in such a way as to mislead; or (b) the tests which he made were not sufficiently extensive to justify him in forming a belief; or (c) he was not justified in forming a belief on the evidence which he examined without probing deeper. Furthermore, he will presumably be liable for any misstatement which may be attributable to the failure of his assistants to take steps which they should have taken even though he instructed them to take such steps and believed, and had a right to believe that they had done so."

Members of our profession are concerned about the possibilities of their being held liable under the Act. They have insisted that they are not experts; that they give opinions and do not make statements of fact and that therefore the consent specified in Section 7 is not required.

It is easy enough for those having no risks to run, for those bitten by reformer's zeal or having a thesis to prove, for those still smarting under losses and for that great body of our public seeking to shift re-

sponsibility for much of their own avarice, to attribute such attitudes to a premeditated program of "Wall Street" to propagandize its rightful responsibility out of the statute. But one facing the reality of the statute's liabilities cannot with equanimity assume its risks, risks which may be out of all proportion to the compensation received, risks of liability which may or may not be based on fault, risks in favor of those who may not have relied upon statements or omissions, risks which may have no necessary relation to losses resulting from misstatements or omissions. It is no answer to the fears of busines men that the courts will give the law a reasonable construction. These men have fairly definite ideas of what are legitimate risks, of what the popular mind, expressed through the courts and juries, will have to say about corporate managements, bankers and capitalists in times of depression. These fears and apprehensions are realities. To be sure there may be some who will be satisfied with assurance from counsel that they have at least an even chance of not being held liable if they act in good faith and reasonably in marketing securities under the Act.

This is certain, there will continue to be financing. Unless some of the more drastic provisions of the Act are modified fundamental changes are apt to develop in securities marketing. It is not inconceivable that much of the underwriting may be done either by the less desirable bankers, of borderline integrity, impecunious, or whose wives will be rich women; or that many more securities will be sold on a commission basis. That firm commitments will be the exception, seems definite. And when firm commitments are demanded the bankers will have to demand almost prohibitive compensation for risks assumed. This will mean corresponding uncertainty to issuing corporations as to marketing their securities and as to the net capital they will get. It is not inconceivable that public financing may have to be done through governmental agencies such as the Reconstruction Finance Corporation. I do not consider this likely, though it has been intimated by some who have been rather closely connected with the Administration.[72]

[72] A. A. Berle, Sr., "High Finance: Master or Servant," 23 YALE REV. 20 (1933).

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