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ADDRESS

of

CHAIRMAN JAMES M. LANDIS

of the

SECURITIES AND EXCHANGE COMMISSION

before

AMERICAN MANAGEMENT ASSOCIATION

at

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You all know what the Securities Act is and what its objectives are to secure for issues publicly offered adequate publicity for those facts necessary for an intelligent judgment of their value. You also know by this time what the attitude of the Commission is towards financing—in the light of this objective of full and fair disclosure to aid the flow of capital instead of to discourage it.

The problem of today springs from the attempt to perfect this attitude. It is the continuing one of reconciling the policy of adequate disclosure with the need of making financing, under appropriate conditions, free from unnecessary burdens. More specifically, that problem—and it is yours as much as it is mine—is to perfect the administrative techniques whereby these two objectives may be reconciled. It will be my effort this morning to deal with some of the phases of this problem in an attempt to look ahead and see what lies within the realm not of promise but of immediate accomplishment.

The expense of registration is undoubtedly a major consideration in the minds of those who are planning to undertake new financing. Let me say at the outset that these expenses have continuously shown a decrease. An analysis of the reasons for this decline will throw light on the possibilities of further reduction of these costs. First, in my judgment, in effecting the decrease has been the improvement in our registration forms. The development both of precision in our requirements and of methods for eliminating irrelevant but costly data, has already been marked. Second in importance seems to be the increasing familiarity of issuing corporations, lawyers and accountants with the process of registration. This has transformed into a matter of normal routine something that initially held all the burdens and headaches of novelty. Thirdly, the amendments to the Securities Act which were adopted in 1934, have eliminated in part the insurance premium charged by experts assisting in the preparation of a registration statement.

One may well ask what expenses are still excessive and what can be done to reduce them. We see several possibilities. One complaint on costs, however, we cannot meet. This arises from enterprises whose entire set-up is so crude and whose operations are so carelessly conducted that they have no right, while remaining in that condition, to seek public investment. And we find many of them, mostly in the promotional stage, so inadequately conceived and so badly supervised that they cannot give even a fairly accurate picture of their present operations or present condition. To reduce cost to meet their complaints and in accordance with their wishes would only mean opening the door to fraud.

Other enterprises, of course, stand in a different category. One great avenue to the reduction of costs lies in the improvement of our registration forms. Last January we took the all important step of differentiating in our requirements between corporations in the promotional stage and those whose past record entitled them to be regarded as "seasoned" in character. Obviously as the record of a corporation's financial experience accumulates, the emphasis from an investment standpoint shifts from organization to operation. The early history of the property account ceases to have as large a significance; facts regarding its promotion become largely immaterial in appraising the present worth of its securities, and similarly the relative value of other information changes. Recognition of factors such as these led to the development of the new form, A-2, the form under which the great refunding program of the current year has taken place.

This is but the first step. There is a further differentiation to be made, one that is already in process and one that I hope will soon be an actuality. This is an effort to achieve greater precision in the requirements and to eliminate irrelevant data by the development of forms appropriate to the class of enterprise seeking registration. The extractive industries, for example, deserve a different treatment from the ordinary industrials. Then too the form should vary with the type of transaction in which the security is to be offered. Sales for cash present different problems than those inherent in an exchange of securities for property. All this implies a less procrustean treatment and a consequent adaptability of presentation to existing methods of operation.

Accounting costs have already shown a significant decline. American business generally seems now to have accepted the theory of the independent audit. This, of course, is the theory of both the Securities Act and the Securities Exchange Act. Our continuing discussions with the accounting profession have brought us to grips with the question of what additional tasks must be assumed by accountants as a consequence of the requirements of the Securities Act. Certain initial costs will inevitably be incurred where independent auditing has not in the past been the customary practice of the corporation. But even here, in exceptional situations, where other adequate checks are available, we have, so far as past financial statements are concerned, permitted a report so safeguarded to suffice. Increases in the cost of audits under the Act, when one clears away certain obscuring contentions, have usually been attributed to three factors: first, the preparation of more complete work sheets so that the accountant can, if subsequently called upon, show that he has made a reasonably investigation; second, the preparation of the various schedules and other supporting data that are required in addition to the general financial statements; and, finally, the amount of time consumed in conferences with the officers of the issuer, lawyers and other officials.

On the first point, the need of preparing more complete work sheets, the accountants now regard this as relatively insignificant. As to the second, the information contained in the required supporting schedules was always drawn up in rough form even before the Act as a necessary step in connection with the preparation of the financial statements. The only additional requirement of the Act is that these rough data be presented in a finished form. The third item -- the time consumed in conferences -- is likely to be significantly decreased as familiarity with the requirements of the Act increases.

Another factor will contribute to a decrease in costs. This is the yearly reporting by listed corporations under the Securities Exchange Act. The corporation that annually meets those requirements will have no difficulty in registering under the Securities Act. The annual statement of its operations will provide virtually all the financial data needed when that corporation next seeks funds in the capital market. Thus, a listed corporation, or a corporation voluntarily assuming the same obligations, now possesses an inherent advantage in seeking new capital. You can be assured that we shall act to further that advantage, wherever possible within the limits of the statute.

To sum up -- immediate progress will lie in the development with your assistance and suggestion of requirements more precise and more adapted to the variety of situations that confront us both. Continuing study to find where any increase in burden exists without a corresponding need for more information will enable a continuing piece-meal reduction in expense -- piece-meal, true, but gradually mounting to significant proportions.

I cannot, however, leave this question of costs without commenting at the same time upon the benefits that have already accrued as a result of the type of corporate reporting that has developed in connection with the two Acts. Clearly, no such comprehensive and accurate picture of American corporate enterprise, its directions, its virtues as well as its defects, has ever before been seen. And if you believe that this material, developed for the protection of the investing public, is merely lying idly on our shelves and not fulfilling its function of slowly but surely transforming us into a nation not merely of security holders but of investors, you need only spend a morning in our shop. Starting a year ago with a small photo-static unit, today we have three shifts at work throughout a twenty-four hour day and a second complete unit is soon to be installed. We now have a daily output of two thousand pages, at a price of from ten to seven cents a page -- an absolute cost price. We supply those who are interested in exhaustive studies, the great statistical services, investment banking houses and investment counsel, banks and insurance companies, great corporations seeking investment for their surplus funds, and very frequently an individual investor.

This leads me to another problem and that is the prospectus. Perhaps, the most common complaint directed against the operation of the Securities Act centers about the length and complexity of the prospectus that under the law must precede or accompany the sale of a registered security. A mere general condemnation of length and bulk because of length and bulk, is the type of outcry that from a constructive standpoint is rather useless. Rather an inquiry must be made into the causes for length and bulk to see to what degree they are justified. To the true expert in investment, facts are all important and the facts that he demands are voluminous, for he is always cognizant of the intricate piece of merchandise that he tries to evaluate. For him even the lengthy prospectus is occasionally inadequate and nothing less than the registration statement satisfies him. I can recall a conversation with a great English financial economist who was delighted beyond measure with a particularly bulky prospectus and bewailed the fact that the English Companies Act produced no such counterpart. Fortunately, or unfortunately, however, he does not represent the average investor. Nevertheless, he and his kind were recognized by Congress as performing an all important function--that of expertly evaluating the security in the first instance and thus influencing throughout the entire line of investment the judgments that persons less learned would acquire as to the self-same security. That class of person, who in large measure dictates the actions of others, must be served and adequately served. To be concrete, he represents the dealer or member of the selling group pondering a commitment, the expert buyer for the large bank or the insurance company, the trustee skilled in his responsibilities, the investment adviser conscientiously weighing the nature of the counsel that he intends to give his clients. These men make no outcry against the prospectus, and their needs must be met for they represent the backbone of intelligent national investment.

A different problem presents itself, however, with reference to the mass of investors, some of whom still believe that surplus is cash in the bank and that balance sheet valuations are readily convertible into money. The great question remains of how to simplify for them a thing that is naturally intricate, and how to do so without running the danger of misleading them by the very fact of an enforced simplicity. Some mechanisms for dealing with this problem have already been employed and others suggested. Some prospectuses, that have passed through our hands, have carried a brief summary of what the underwriter deems to be the salient facts upon the front page in the hope that even the laziest investor will read at least one page. Some have carefully refrained from the common legal failing of prolixity and succeeded in being succinct and clear. One suggestion, that certainly deserves important consideration, is that the Commission should act under the powers granted it by Section 10 of the Act and provide for a type of brief prospectus for the average customer who, at the same time, if he so chose could demand the fuller expert type of prospectus. Indeed, the very right given to the Commission to classify prospectuses according to the circumstances of their use may well be deemed to argue that the Congress contemplated some such action.

Recently, the Commission provided by regulation for certain types of newspaper prospectus in the hope that offerings of securities would be announced in a less bare fashion than is the present practice. Actual tests proved that the regulations permit advertisements comparable in scope to the better advertisements in use before the Act. Newspaper advertisements of this type have not, however, appeared. One explanation, of course, may be that recent markets have been sellers' markets and thus advertising has been considered an unnecessary luxury. But examination also indicates that hesitation as to the use of these offering announcements also springs from some vague fear of liability consequent upon their use, because of the fact that all the material facts are not stated in the advertisement. The occasion for such a fear is beyond our legal understanding. That material facts are omitted is patent from both the regulation and the advertisement. Who would deny that the recent financial record of the corporation is a most material set of facts? And yet the regulation permits its entire omission. Obviously, the omission of material facts was designedly implied by the very power granted to the Commission to classify prospectuses under Section 10. And if there be the slightest doubt upon that score, the very regulation of the Commission by force of Section 19 protects any person from liability who acts pursuant to its direction.

One further brief problem -- The Act, as you know, provides for a lapse of twenty days between the time of filing and the effective date of registration, that is, the date upon which the security can first be legally offered. The purposes of this period were primarily -- one, to permit examination of the statement by us and correction of its patent defects before offering or, in default of such correction, the institution of proceedings to prevent sale of the security. The other purpose was to provide for more orderly and less feverish distribution of the security, in the thought that this twenty day cooling period would permit wide dissemination of the basic facts regarding the security prior to the time when commitments could be made. Considerable question arises as to whether the second purpose has been effectively realized and whether some of the by-products of that mechanism are not matters for our serious concern. I cannot on this occasion take the time to analyze this situation. But it seems to me that you should be made aware of the factors that have and will tend to make for delay in the twenty-day period.

Delay beyond the statutory period can hardly, if ever, be charged to us except in cases where adequate reason for that delay existed. Indeed, on occasion we might well be criticized for not delaying beyond the period, when underwriting and price amendments frequently reach us a mere twenty-four hours before the date of public offering. Delays, where they occur, spring from a variety of causes of which several are outstanding. Chief among these is pure carelessness in the preparation of data. The act of registry called for by the statute is as solemn as should be the act of seeking the safeguarding of other people's money. Carelessness and

inadequate preparation in the undertaking of such a venture should never be countenanced. Again, delay arises from an unwillingness to meet the test of full and fair disclosure. Criticism arising from delay due to such a cause, is, of course, real praise. Recently, however, certain public offerings have encountered delay for a reason that gives us great concern. The very nature of the offering itself - for example with outstanding options, sales to be effected against market quotations, often accompanied by an agreement to withhold for a specified time from the public market an overhanging large block of stock - is perfectly adapted for traditional manipulative tactics. To expedite such an offering without a thorough investigation of whether manipulation has indeed already begun or is in preparation, would justly bring discredit upon the administration of the Act. And investigations of this character are both lengthy and burdensome. We can and do meet justifiable demands to meet an offering date on schedule, and you can be assumed that the instances when delay is incurred normally arise from some factor that should never have been permitted to enter the planned offering in the first instance.

There are other significant situations when the betterment of our administrative techniques can be hoped for, but on this occasion I can only deal with a few facets of our many sided problem. If, perhaps, I have given you some sense of the complexity of the issues that confront us, some idea of the temper and the atmosphere that governs our handling of them, and evoked from you a consciousness that a frankness and sincerity in criticism is a thing that we welcome rather than abhor, I shall feel satisfied with my morning's endeavor. It is a serious, continuing task that confronts us, one in which we have some pride in having cleared a portion of the road, but also a consciousness that the road, truly to carry out the unquestioned purposes of the Act, must be a King's highway that all who seek it can follow.