

Address of Judge John J. Burns
before the
INVESTMENT BANKERS ASSOCIATION - New England Division
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And now it can be told. That would be an intriguing title for my remarks, except that apart from the mathematical result, the implications of the Presidential election depend pretty much on the predetermined view of the prognosticators. Organized labor claims it has a victory for its principles. The left wing of the Labor Party sees in it a vindication of its position. To many the principles of WPA seem to have conquered. To some thoughtful people there has been an endorsement of liberalism by the great majority of American people. No one can be sure except of this one thing--that we have had an amazing vindication of the processes of democracy.

Just think of the emotional experience which it has been for many Americans, aided and abetted by a press hysteria of unusual proportions. The truth of the matter is that prejudices were so aroused during the campaign, even on issues where reasonable men might differ, that pleasant personal relations were threatened by the political passions so aroused.

As election day drew near the atmosphere appeared to grow more reasonable, more rational, more temperate; and after so many American citizens had registered their desires, their judgments, their passions, their views, their affections and their dislikes at the polling booth, a

complete transformation took place. On Wednesday morning America had the sign out--"Business as usual"--if anything a trifle better. To be sure, sour faces were substituted for bright sunflowers, but a great social fact was the good humored sportsmanlike acquiescence in the rule of the majority.

Not only did a zealous political party and its campaign managers recognize the will of the majority in a wholesome and fresh spirit, but the defeated candidates themselves, their most articulate representatives, all bowed to the essentials of our American system.

I think we can all be proud that on this occasion when the American method was put to such a severe test it should be so singly successful. No hard feelings, no reprisals--the will of the majority prevailed and this in one of the most tempestuous social times of our country's history.

In a world divided sharply on class lines where, as the late George Chesterton pointed out, the only recent contribution at least in Europe to political philosophy was the discovery that one need not convince his opponent but may meet his arguments by beating him, and if necessary imprisoning him, or possibly assassinating him, the American way of adjusting in orderly fashion through a free press and a free ballot the difficult problems of human relations

is in truth an inspiring thing. I have heard a few competent critics venture the judgment that this display of successful democracy in action may mark a swing of the pendulum all over the world back to a liberal philosophy of democratic government.

For the Securities and Exchange Commission the election, to be sure, had great significance. You have probably observed that no Commissioner took an active part in the campaign nor, for that matter, did the members of its staff. I feel quite sure that you will applaud this attitude of impartiality in a heated campaign. The Commission is, after all, a quasi-judicial body possessing important powers of judgment regarding interests of tremendous value. In a sense, participation in the political arena by the Commission would be analogous to campaign activities of a federal judge on behalf of the administration which had appointed him. The Commission wisely felt that not only is it important in this country that strict impartiality be preserved but that nothing be done which would cause the appearance of partisanship. I am sure that the action of the Commission in this the first national campaign after its creation, will establish a precedent which will endure.

Not one of the three Acts which the Commission administers was involved as an issue in the campaign. To be

sure there was general talk about regimentation and one heard every now and then of the perils of the American system and the growth of centralized bureaucracies, but no one in a responsible position in the campaign came down to cases and made an issue of the Acts committed to the care of the Commission. Of course, the President and his Democratic platform regarded the legislation as accomplishments to be taken as part of his record on which he sought the people's endorsement.

The Republican platform endorsed almost in terms the Securities Act of 1933 and the Securities Exchange Act of 1934. It also approved of regulation of the interstate activities of public utilities leaving that question of what is interstate activity pretty much in the air. Governor Landon, however, speaking in Portland gave an unqualified endorsement of the first two Acts as representing sane, orderly and progressive examples of federal control. It might also be mentioned that in his Portland speech the Governor spoke his approval of the Public Utility Holding Company Act of 1935 with the result that not only in the framing of the platform and in the speeches of the candidate, but also through the complete silence on the subject on the part of the prominent spokesmen for the opposing party the conclusion is compelled that the legislation administered

by the Commission was deliberately taken out of the realm of popular issues in the campaign.

On the other hand, there is hardly a person here who would dare urge that this legislation, sponsored by the President and passed by the Congress, is not to be regarded as having received the seal of approval of the American people through the amazing vote given to the President last Tuesday. I have no hesitancy in stating that federal regulation of public offerings of securities and of trading on exchanges and in the over-the-counter markets, so far as political approval of the American people is concerned, has come to be regarded as a permanent part of our governmental system.

So far as the '33 Act and the '34 Act are concerned, and these after all are the principal concern of your group, all thoughtful men must recognize the apparent inevitability of this type of regulation, when it has been so completely foreclosed as a political issue, particularly when it is considered that not a single federal court which has passed upon this legislation has regarded either Act as violative of the Constitution.

One of the generally admitted principles to be derived from the American political experience is that a President who is reelected is likely to accomplish more in the way of good government, is more likely to inaugurate a

better administration, to consolidate social gains more effectively, than in his first term.

And this, in turn, is due to a principle of the unwritten Constitution, no less effective than the written document, that one man may serve not more than two terms. The human factor explains how much more detached and less politically inclined a second term executive is likely to be. As some would phrase it--it is a delayed bid for immortality. That, of course, is not a hard and fast rule but it is a safe generalization that political considerations are less likely to weigh heavily after the fourth year. I do not intend to convey the idea that the millenium will come at the beginning of the President's fifth year because no government can avoid rule by compromise, but it is safe to assume that the government will devote more of its time to proving the administration. Considerable progress has been made in the first term in pointing out the lines of social advance. The President's program for reform has been far-reaching. There now remains a great task of improving the highway toward the goal of reform--the bumps must be smoothed out, the sharp curves must be eliminated and the detours made unnecessary.

In an analogous sense the same thing is true of an agency administering reform legislation. The lines of

advance must first be laid down, and later there must be a process of adjustment to see that a higher degree of efficiency is attained. In that respect I should like to call your attention to some of the qualities of administration which those of you who have had contact with the Commission already know. In the first place, the Securities and Exchange Commission has been quite cautious. By that I mean that the Commission has recognized the risk of precipitous regulation to a financial machinery which is sensitive to change and unschooled in outside disciplines. In the second place, as a corollary of its attitude of caution, the Commission has never sought to impose regulation without adequate information. This is but a recognition of the actual necessities of a valid legislative process. The third quality of its administration has been the desire of the Commission to seek active cooperation from agencies like your own to the end that the law will attain its objectives without undue annoyance or friction. This is true not only in the field of enforcement, where your cooperation can be of great assistance, but also in the field of regulation.

In the field of enforcement the Commission has been aided materially by the assistance rendered to us from various sources. It has not been unanimous. We appreciate that many of the members are not intrigued of the prospect of assuming the role of an "informer". On the other hand,

an appraisal of this request for cooperation, viewed selfishly and in the light most favorable to your own business, would seem to dictate the necessity of active cooperation with the Commission to the end that the outlaws in the trade be eliminated. In a business so competitive it is a part of wisdom first to have standards established, and secondly to have an efficient enforcement of these standards against those who would make competition a process of lowering standards.

It is in the field of regulation where your aid is particularly valuable. As you know there are still a number of difficult problems affecting your business on which the Commission has not exercised its regulative powers. These include rules for the regulation of pegging, fixing and stabilizing operations, both on exchanges and in the over-the-counter markets; rules for the regulation of puts, calls, straddles and other operations; rules relating to borrowings and solvency of exchange members, brokers and dealers, and to their hypothecation of customers' securities; rules relating to the registration of unissued warrants and unissued securities for when, as and if issued trading on exchanges; and rules dealing generally with manipulative, deceptive and other fraudulent devices or contrivances in the over-the-counter market.

The problem of issuing rules regulating pegging, fixing and stabilizing has been extremely difficult. It is our hope that in the very near future the preliminary draft will be available for criticism. As you know, the whole problem of pegging gave

the Congress great difficulty. In one sense it is the reconciling of what appears to be irreconcilable factors, the paradox of preventing deception by allowing a little deception. When one's ideas are fixed the problem of committing them to language which will be, at one and the same time, clear and yet not subject to evasion is a task that calls for a most skilled type of draftsmanship.

In this field, as in so many fields where the Commission must act there is, on our part a great urge to lay down general principles and standards because evasion is most difficult, whereas, so far as the men on the street are concerned, they want particularization, they want certainty; they do not want, if they can help it, to be subject to the judgment of the Commission as to whether certain conduct is within or without a given standard.

This clash between the need for certainty and the need for elasticity is found everywhere in the law. I recall Dean Pound's speaking about the law of unfair competition, pointing out that the English Chancellors insisted that the law be declared in very general terms because when they had been specific the ingenuity of competitors would be devoted to devising methods of evasion.

One of the most difficult problems presented to the Commission arises out of the amendments to Section 12 and Section 15 of the Securities Exchange Act of 1934. As you know, this Act continued unlisted trading privileges on exchanges for securities that had enjoyed them at the time of the amendment last May. It also

granted to the Commission the power to admit to unlisted trading privileges on national exchanges securities which had been listed and registered on another national exchange, and a third category included any security in respect of which there was available from a registration statement periodic reports or other data filed under either Act, information substantially equivalent to that available in respect of a security registered on a national securities exchange.

Under the law, when an exchange seeks to admit any new security to unlisted trading it is up to the exchange to show to the satisfaction of the Commission that there exists in the vicinity of the exchange sufficiently widespread public distribution of and sufficient public trading activity in the security to render the admittance to unlisted trading necessary or appropriate in the public interest or for the protection of investors. The statute also provided that no application to extend unlisted trading privileges to the third category (that is, those not listed on a national exchange but where there is on hand information comparable to that available in the case of a listed security) "shall be approved except upon such terms and conditions as will subject the issuer thereof, the officers and directors of such issuer, and every beneficial owner of more than 10 per centum of such security to duties substantially equivalent to the duties which would arise pursuant to this title

if such security were duly listed and registered on a national securities exchange; except that such terms and conditions need not be imposed in any case or class of cases in which it shall appear to the Commission that the public interest and the protection of investors would nevertheless best be served by such extension of unlisted trading privileges."

The Commission is also given powers to suspend or terminate trading in such securities if it is found after hearing that there existed inadequate public trading or that because of the character of the trading such termination was necessary for the protection of investors.

Many have regarded these amendments as granting the Commission the power to mould the security trading business of the country to a preconceived pattern. This is a misconception. The statute attempts to regulate competition by providing a fair field with no favor. The Commission in protecting the public interest has the duty of protecting the field of competition among exchanges, and between exchanges as a group and the over-the-counter markets. As the report of the Senate Committee on Banking and Currency phrases it-- the amendments are intended "to allow each type of market to develop in accordance with its natural genius and consistently with the public interest.

The task of spelling out where the emphasis is to be placed, what considerations are to be controlling, in making a body of

precedent which will be in conformity with the statute and at the same time realistic in its effect upon the various types of trading is indeed an impressive task. The need of cooperation cannot be exaggerated. If time would permit I could discuss profitably the implications of the amendment to Section 15. Instead of limiting registration of brokers and dealers to those who make or create an over-the-counter market or use the facilities of such a market (whatever that meant), Congress has imposed a licensing system on all brokers and dealers with relatively few exceptions who use the mails in the conduct of their business. This has been a grant of tremendous power to the Commission. In addition to its power to deny and terminate the license where a person has been convicted of a crime involving a security transaction, where an injunction has been issued regarding a security transaction, where a stop order or other similar order has been in effect against such person, the Commission is now empowered to deny, suspend or terminate where there has been wilful violation of its rules and regulations. It has also been given the power to define manipulative practices in the over-the-counter markets.

While the definition and detection of manipulative practices on the exchanges is no easy task, at least there has been a considerable amount of information on the subject. In the

over-the-counter markets, or as one was called it--the under-the-counter markets-- there is much darkness. The Commission has the task of finding out the evils, seeking the remedy and phrasing it in a way which will reach the evil and not impose an undue burden upon the innocent. There is a field of administration where your cooperation may be said to be vital. After all, you as a group know the evils, you as a group know what practices even though undesirable ought not to be the subject of governmental regulation. You know where excessive zeal may bring unfair results. You would be in a position to give important advice on the issue of whether language should be general, imposing broad standards, or specific, imposing particularized prohibitions.

By the amendment which is now known as Section 15(c) any broker or dealer who makes use of the mails or the instrumentalities of interstate commerce to effect any transaction or to induce the purchase or sale of any security (other than commercial paper, bankers' acceptances, or commercial bills) by any manipulative deceptive or other fraudulent device or contrivance acts unlawfully. Such a person is subject to the civil and criminal liability provisions of the Act. The Commission is ordered to define by rule and regulation such devices and contrivances as are manipulative, deceptive or otherwise fraudulent.

On that sub-section two observations are pertinent.

First, that the section applies to all brokers and dealers whether registered or not in all kinds of security transactions unless the particular security is specifically exempted. Thus it applies to transactions by dealers and brokers in municipals. Secondly, the Commission is charged with the duty of resolving this general phrase "devices or contrivances as are manipulative, deceptive, or otherwise fraudulent" into definite prohibitions of specific conduct or at least adopting standards which are less general than the language of the statute.

And now a final word. There is really between your association and the Commission no antagonism. That may sound bromidic but it is true. In fact I believe that the Commission has been a significant factor in restoring public confidence in the investment business. I recognize that some may disagree with me, but there are many among you who will echo my judgment.

The Commission already has a tentative program of practices to be considered in the light of its duty of definition. On this agenda which is now receiving the attention of our staff are such practices as (1) spreading false rumors, (2) fictitious sales, (3) fictitious quotations, (4) excessive markups, (5) selling at market where no market exists, (6) payments to customers' men for buying power, and other similar matters.

We are receiving the assistance of your representatives in the Investment Bankers Conference Committee. I do not hesitate to praise that assistance and speak in high terms of its present

and future value to the Commission. I am just as enthusiastic about its actual and potential value to your own fraternity.

The Conference Committee following the trend of big business has had itself incorporated in Delaware and is actively seeking as representative a following as can be attained. It is worthy of nation-wide support not only from the viewpoint of the trade but also in the larger perspective of the public interest.

It takes but a statement of our program to convince one how essential it is that in the promulgation of standards, prohibitions, and in the other activities of the Commission, the best brains and the most respected among you have a standing with the Commission for active cooperation and mutual guidance.

The success of all of you rests upon the particular factor called, for want of a better name, "good-will", which depends on the creating and fostering of public confidence in the fairness and honesty of your methods. Because of this I assert that in the horizon of your business tomorrow the Commission is bound to play a leading role.