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COOPERATION WITH STATE SECURITIES ADMINISTRATORS

An Address By

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It is a gratifying experience for a Federal Bureaucrat to make a speech to a group of distinguished state officials. It shows that in spite of the tug of war between state and federal authority, the people on both ends of the rope are still on speaking terms.

I feel a particular affinity for the National Association of Securities Administrators. The first substantial legal work I ever did in the securities' field involved the blue sky qualification of an unlisted common stock of a large oil company. The company was and is a substantial one, but at that time its stock, being both unlisted and an oil stock, the qualification in some 25 states presented all the problems in the book. I learned what I know about your business the hard way.

Rather than talk to you on some of the detailed problems of state and federal securities' regulation, I would prefer to speak

in my character as an unquestioned expert on the early life of our host Administrator, J. Edwin Larson. I knew him when! The only deterrent to full and frank disclosure on the subject is that he knew me when! Hence the silence of an uneasy peace. We both have the bomb. Ed and I are fellow Pennsylvanians. He came out of Forest County to Allegheny College, Meadville, Pennsylvania, back in 1919. He was just a country boy then, but he learned fast. By the time he was a Junior he was running the student body, and when he was a Senior he ran the college. Incidentally he and I were the proprietors of an establishment called the "students' suititorium." We had a fine pressing machine (I can still smell the gas fumes) which was guaranteed to press the spots in. If any of you are having trouble with the valet service here at the hotel give Ed a ring. We had planned to set up shop again. The unanticipated necessity of my

getting back to Washington has compelled me to turn over to him my interest in the projected enterprise.

Oh, yes, I would like to put in another plug for Allegheny College. Ray Cox of the Pennsylvania Commission is also a graduate of that institution. Then I have a more recent tie to your Association. One of your ex-presidents, Clarence H. Adams, whom we all know as "Ted," has been serving on the Federal level now for a year and a half. Ted is a sound, sensible, cooperative fellow Commissioner if there ever was one. He has an ability in penetrating and accurate analysis which makes him a great source of strength. He can cut through the brush pretty fast. He has a tremendous storehouse of experience, upon which those of us who are newer to the business draw daily.

In the few speeches I have made since becoming Chairman of the SEC, I have spoken in considerable detail about our programs.

Today at this opening session that kind of talk is probably not quite so much in order. Ted Adams will be active in a forum Thursday and Bob McDowell, our new Director of Corporate Regulation, will present tomorrow in some detail some of our mutual problems in the matter of investment companies. I'm very sorry that some pressing matters back in Washington make it absolutely impossible for me to remain here to work and play with you for the rest of the week. It would have been both a pleasurable and profitable experience. Washington isn't the United States as Paris isn't France, and I know it would have helped my perspective a lot to have participated in your discussions and gotten to know you all better.

In order to facilitate the development of mutual understanding of our common problems, we have a sizable SEC delegation:

here in addition to Ted Adams and Bob McDowell: Bill Green, the Regional Administrator in Atlanta (Bill will you stand up); Walter Holden, Assistant Director of the Trading and Exchanges Division in charge of the enforcement section (Walter stand up);. May I say that the members of the Securities and Exchange Commission, everyone of them, those here with you today, plus Paul Rowen of Massachusetts, Sinclair Armstrong of Illinois, and Jack Goodwin of Alabama, are hard-working people whose first thought is to do a good, sound, sensible, alert, and workmanlike job of administering the statutes committed to their jurisdiction.

Instead of talking too much about details, I am suggesting that for a moment we get off to one side and look at our work in perspective.

Miami Beach is a magnificent place to go in order to get off to one side. The difficulty is to keep looking at our work. There is too much else to look at.

We all belong to the group known as regulators. Nobody loves us. There is something fundamental about that feeling. In the coupled thought expressed in the phrase "liberty under the law," liberty is by far the more popular member of the couple.

Free enterprise is the economic aspect of liberty. Free enterprise needs capital to keep it going. In the case of established, mature, progressive businesses we have conservative minimum-risk investment. In the case of many other businesses, the investment is truly risk capital. In some instances the investor is throwing his money away. Our work has to do primarily with seeing to it that the investor at least understands what he is getting into. Nobody seriously contends that we shouldn't have any securities' laws. It is a question of what kind and how they are enforced. We need risk capital. In the life time of all of us, small companies have grown into industrial giants. Whole new industries have sprung up -- radio, television,

aircraft manufacturing, air lines, bus lines, pipe lines, chemicals, synthetics, electronics. The use of automobiles, tractors, telephones, gas and electricity has multiplied many fold. There have been a lot of false starts in every industry. Some were unlucky; some lacked managerial ability; some lacked good engineering; some were unconscionable promotions; some were squeezed out by competition. Yet the net result over the years has been growth and progress.

Whatever techniques and expedients are employed to take care of periods of economic distress the ultimate salvation of the American economy comes from the development of new industries and the expansion of existing industries. Just look at some of the industries I mentioned a moment ago and compare them with what they were twenty years ago (if indeed they were in existence twenty years ago).

The growth and progress of our industrial strength requires a continuous process of capital formation. Cash in the cookie jar,

or under the mattress, and \$100 bills stored in a safe deposit box produce nothing. An Indian Maharaja with a fabulous fortune in jewels represents static wealth. Our system here works because it does entice people to put their savings to work in industry and commerce.

Investment by the public generally is a Twentieth Century phenonemon in the United States -- and more recently Canada. The rush of people to get into the securities market is as significant an economic and social development as the rush to settle the west. That great movement of population changed the face of the nation, but it created many problems: simple law and order; Indian rights; homestead policy; water rights; fence laws; statehood, reclamation; and irrigation. The problems were and are complex, controversial, and some of them still aren't solved. The economic movement of

the general public into the capital markets also created problems. The states were the pioneers in their solution. Each state sought to curb the kind of evils which were near at hand. Consequently, the laws differed widely and the goal of a uniform state securities' law is still beyond the horizon. The interstate character of this surging economic movement caused the enactment of federal securities laws, and we do not have all the answers yet. Let's remember though that we are dealing with a great economic movement that, like the settlement of the West, is changing the face of the nation.

Whatever we do in this task of regulating the sale of securities, let us always keep asking ourselves whether we are helping or hindering the growth of the American economy.

The field of legitimate investment, of course, covers every classification from speculations to blue chips. There is an

area, however, outside the range of investment entirely. That area I spoke of a moment ago as "unconscionable promotions." Another term is "stock swindle." Every dollar taken in a stock swindle is a dollar that should have gone into legitimate investment. If our activity stops swindles, labels speculations for what they are, and provides for public disclosure of basic information concerning the issuers of all publicly offered securities, our job is well done.

We have our statutes to work under and you have yours.

In the administration of these statutes we have varying degrees of discretion. The sound exercise of that discretion calls for good judgment. To the extent that our processing of a registration statement or an application for a permit results in adequate disclosure and culls out fraud and misrepresentation, it is good. To the extent that it results in a lot of needless paper work

and delay we serve no useful function. The accuracy with which we draw the line between the two is the test of the soundness of our administration.

There are many areas in which you are interested in our judgment and we in yours. I want to mention a few of them.

Last year the Commission put out a rule providing for an identifying Statement as a means of disseminating information about proposed offerings. That presented challenging questions to many of you. But the net result of a year of cooperation and discussion has been progress in the mutual adjustment of our regulatory scheme with yours in the use of this medium.

We're working as you know on a reexamination of a number of our rules, some of which may change the scheduling of what you sometimes refer to as the S.E.C. release.

For example, we have circulated for comment proposed rule changes under the Public Utility Holding Company Act and under the Securities Act, which will in almost all competitive bidding cases make unnecessary under either Act supplemental orders prior to a reoffering by underwriters. Under the proposed procedure, the final amendment to the Federal registration statement will become effective without order when it is filed in Washington or in a regional office. This would result in final effectiveness in most cases within a few hours after bids are opened. While most competitive bidding issues are exempt from most blue sky laws, we did not think that even as to the non-exempt issues, the new procedure would create any particular difficulties in obtaining the usual prompt telegraphic blue sky clearance. If any of you feel that our proposed rule changes should be modified to mesh more closely with state requirements, your

comments would of course be most appreciated.

On September 28 of this year I sent to our Regional

Administrators a letter reading, in part, as follows:

"In response to my call dated August 12, 1953 for additional suggestions as to ways and means to save manpower, four Regional Administrators suggested in one form or another the turning over to state authorities of cases being investigated by SEC in which the facts developed indicated an offense more readily provable as a violation of state law than as a violation of any statute administered by the Commission.

"This suggestion, which is in conformity with the Commission's policy of cooperating with the states, will be carried out.

"Accordingly, in the case of investigations, except formal investigations specifically ordered by the Commission, each Regional Administrator is authorized, on his own initiative, to make available to the appropriate state authorities all material dealing with a pending investigation where:

- "(1) an investigation discloses there has been a clear violation of state law, and
- "(2) it appears that there will be substantial difficulty in proving the suspected violation of the federal law, and
- "(3) the Regional Administrator has reason to believe that the state authorities will proceed promptly to complete the investigation and enforce the state law.

"Moreover, in the case of formal investigations which have theretofore been specifically ordered by the Commission, each Regional Administrator should, under the circumstances outlined

in the previous paragraph, recommend to the Commission the turning over to state authorities of the material dealing with such investigation.

"Where documents or statements are released to the state authorities for their use, the Regional Office should obtain an appropriate receipt in reasonable detail.

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"It is contemplated that the Regional Administrator will make a determination whether to turn over, or recommend turning over, a case to the state agency at the earliest practicable stage of the investigation. After a case has been so turned over, the Commission's further efforts on the matter should be limited to acting in a consultative capacity on request. Such requests should be honored if the nature of the offense or its geographical scope makes the use of the Commission's facilities of substantial help in completing the investigation and prosecution. Following this procedure should save time and personnel, permit more expeditious handling of the investigative case load and lead to better law enforcement."

That letter meant what it said. If is, of course, however, inherent in the situation that the Regional Administrator, or the Commission, or both, must exercise judgment and discretion in each particular case. Moreover, whether you take such a referred case depends on your judgment and your respect for ours.

Your liaison Committee has been working with us on the subject of broker-dealer inspection programs. We now have in summary

form information as to what states have what inspection programs.

We hope that out of this will come some coordination of effort which will increase the number of broker-dealers inspected. By cooperation in the matter of scheduling alone it should be possible to cut down both the number of uninspected registrants and the number of over-inspected registrants.

Truly significant progress is being made in the matter of Canadian offerings. The only formal vehicle for cooperation between Canada and the United States in the matter of securities law violations is the Supplementary Extradition Convention of July 1952 which amended the existing treaty so as to include, in effect, securities fraud by the use of the mails.

This amendment has stimulated welcome cooperation of both public authorities and trade organizations on the provincial, state

and federal level. Commissioner Adams will present to the forum additional and encouraging information as to the help which has come from many fine people.

I have discussed very superficially these few matters illustrative of the problems in which you and we are called upon to exercise our judgment and to do a little accommodating back and forth. The discussion tomorrow on investment companies and the forum on Thursday, as well as the intervening unscheduled bull sessions, will provide an opportunity for thorough, frank, and gloves-off exchanges of views.

Progress in doing the job we have to do is always going to be relative. There never will be a system in which, as a result of your good work and ours, every investor will be assured of

dividends, plus return of capital, plus capital gain. I only hope, as I am sure you hope, that over the years we can administer firmly and sensibly laws which provide the investor with adequate information as to what he is getting for his money.