

Address of

ROBERT I. MILLONZI, COMMISSIONER
UNITED STATES SECURITIES & EXCHANGE COMMISSION

To The

Buffalo Chamber of Commerce
Buffalo, New York
February 20, 1952

When Clif Fichtner talked to me about coming to Buffalo to discuss some aspects of the work of the Securities and Exchange Commission, I told him I was happy to accept as a paid-up member of the Buffalo Chamber of Commerce. I had hoped it would also present an opportunity to come here with my friend, Harry McDonald, who comes from Detroit so that I could prove to him that Buffalo was originally chosen as the site of the automotive industry and that Detroit only got the business after we had turned it down.

Finally, this occasion gives me an opportunity to discuss with you some of the work that the Securities and Exchange Commission has been doing in the interests of the investing public, particularly as it refers to Canadian securities.

We on the border are more familiar with Canada and Canadians than the people in the United States who have not had an opportunity to go into Canada frequently and to meet many of its people. For several years I have lived for a good part of the year in Canada, and as a result, when some of the Canadian problems are discussed at the Commission, I have found that this familiarity with the country and its people has been very helpful to me. People who come here from all over the world are amazed at the cordial and friendly relationships we have maintained with the Canadians and at the fact that we have a continuous unfortified border, with people of both countries moving back and forth at will.

For a long time, our feeling toward our Canadian neighbors has been that of a big brother toward a small brother. Because we had such a large population in comparison with theirs and our industrial might was so overpowering, we, quite naturally, came to form some ideas about the relative industrial and political strength of our two nations. It seems to me that we are going to have to revise our thinking quite drastically. Canada is no longer a small factor in our economy, nor is it a small political factor in the world of nations. We all know of its vast untapped natural resources, and many have been heard to describe it as the "last frontier." It is evident that the amount of capital that is now

attracted to Canada is substantial by any standard of comparison. There are many indications of this. The Canadian dollar, in the eyes of the free markets of the world, is as good as our dollar. The national income of Canada exceeded 21 billion dollars last year, and it will be greater during the current year. The Canadian economy is no longer based solely on natural resources and wheat. It is much broader and there are evidences of industrial strength which is being gradually diffused throughout all the provinces. Thus, we find in Canada the manufacturing of practically everything that is being made in the States. New industrial plants are being erected for textiles and plastics. The development of hydro-electric power is another of the great advances being made in Canada, and it will provide adequate and cheap power for the manufacture of aluminum, among other things. In fact, the largest aluminum establishment in the world is now being constructed in Western Canada. Canada has iron ore, precious metals, timber and newsprint among its many resources.

This expansion has made necessary the extension of existing railroad lines and road systems. New areas containing oil reserves and natural gas have been discovered and are being developed.

Their standard of living is the same as ours. Canada is certainly a weightier factor so far as the American economy is concerned than ever before, and the growing interdependence of both our countries will be of major significance to the future of both.

This could not have been accomplished without capital. Formerly, it was to the British that the Canadians looked for this commodity, but in recent years it has been the United States that has supplied the major portion of foreign capital for Canadian ventures. According to a recent issue of the United States News and World Report, the United States is now pouring 750 million dollars a year into Canadian iron ore and oil developments and into its factories and utilities. The American stake in Canada now totals almost 6 billion dollars. It is interesting to note that the biggest investors in Canada are the Canadians themselves. In the last year it has been

estimated that they put $4\frac{1}{2}$ billion into their own economy, which amounts to approximately 22% of their natural income. Americans do have a large stake in this vigorously expanding Canadian economy, and it can be expected that our citizens are going to put more money into Canada as time goes on.

Now let us pass on to the general problem of securities and our securities laws in relation to this general topic.

The Securities and Exchange Commission administers several statutes in the general field of securities and finance, all enacted by Congress for the protection of the interests of investors and the public.

Securities are by their very nature much different from any other type of "merchandise" for which there are established public markets. A person who wishes to purchase a new car or a household appliance -- or for that matter, a peck of potatoes or a bag of beans -- can pretty well determine from personal inspection the quality of the product and the reasonableness of the price in relation to other competing products. But this is not so with respect to a bond or a share of stock.

For example, an engraved certificate representing an interest in an abandoned mine, or in a defunct gadget manufacturing company, might look no less impressive than a "blue chip" security with a history of years of unbroken dividend payments. Beyond that all comparisons cease -- and for the average investor to differentiate between the securities of little or no value and those offering at least reasonable prospect of a satisfactory return on his investment requires (1) a personal inspection of the properties and operations of the issuer (which, for all practical purposes, is impossible) or (2) that he rely on what others tell him about the company.

Recognizing this and the further fact that traffic in securities often extends across State lines, thus restricting the ability of particular States to suppress fraud in their sale, Congress enacted the "truth in securities" laws to protect investors against misrepresentation, manipulation and other fraudulent acts and

practices in the purchase and sale of securities. Congress also sought to establish and maintain just and equitable principles of trade in the securities markets and thus to reestablish investor confidence in securities as an investment medium and to revitalize our capitalistic economy.

It should be understood that the securities laws were designed to facilitate informed investment analyses and prudent and discriminating investment decisions by the investing public, and that it is the investor and not the Commission who must make the ultimate judgment of the worth of securities offered for sale. The Commission is powerless to pass upon the merits of securities; and assuming proper disclosure of the financial and other information essential to informed investment analysis, the Commission cannot bar the sale of securities which such analysis may show to be of little or no value.

It is hoped that the following discussion of the nature and scope of the Commission's work and authority will contribute both to a better understanding of the laws, and, in turn to their objective of investor protection.

The Division of Corporation Finance of the SEC in Washington is ever vigilant to the extravagant claims and unsupported blandishments that have been attendant upon stock promotions in the past. A prospectus meeting certain statutory requirements must be used in connection with the sale of new securities. Generally, similar information must be made available to the public with respect to all stocks that are listed on national stock exchanges. Stockholders are also protected with respect to proxies and claims made therein in the solicitation of stockholder votes. As a result of the securities laws and the administration of these laws by the Securities and Exchange Commission, there have developed in the United States some well-settled patterns of business conduct which are generally conceded to be all to the good.

In Canada, there is regulation of a kind, but it does not conform specifically to our own. Now, there are people who break securities laws in the United States,

and there are people who are doing the same thing in Canada. Indeed, many of the law breakers went to Canada after the Securities Act was passed and started operating there. As we know from our many investigations, a considerable number of the illegal operators in Canada are Americans. The amount of money that has been taken from the investor is gigantic. Various writers who have studied the situation both here and in Canada have stated that perhaps a million dollars a week has been invested in fraudulent promotions. The exact amount is, of course, unknown; but I have been advised of one spot-check made by a government agency which showed that over a tested two week period $3/4$ of a million dollars had been taken. This is money that could have gone into legitimate industrial Canadian enterprises. Indeed, it has been stated that man is the only animal that can be skinned more than once.

In approaching the problem of Canadian securities, it must be realized that we are dealing with a problem that is common to both countries, and that it would be unfair to label all Canadian securities as disreputable or fraudulent. Unfortunately, they have been getting that reputation as the result of the activities of a small group of confidence men operating almost exclusively in Toronto, and conducting their promotions in this country through the use of the mails and the long distance telephone.

Actually, by far the greater amount of the American capital that is exported to Canada goes into legitimate investment channels. Much of this investment is by American corporations having subsidiaries or other interests in Canada. A good deal of it is by knowing professionals, acting individually or in small syndicates, who are well able to take care of themselves. It is another great source of capital -- the savings of the average, middle-class American -- that has been tapped by the unscrupulous mail racketeers, and one of the unfortunate results has been a drying up of that source as far as legitimate Canadian business is concerned.

I think that everybody in this audience has heard about the activities of the mail racketeers, and the statistical probability is that some of you have heard

about these activities directly and painfully. The examples of fraudulent stock promotions are many and lurid, and there is no useful point in relating any of them individually. Suffice it to say that they occur frequently both in the United States and in Canada.

The victims of the promoters are in the most cases unsophisticated persons of modest or straightened circumstances -- because such persons make the easiest marks. Our investigations have shown that the small amount of money that actually goes into the enterprise is insufficient to develop the property, so that even if the property has potentialities, they are never realized -- at least we have not found a single case where a promotion thus conducted has been a commercial success.

It is to be emphasized again that such practices are not typical of Canadian securities dealers generally.

We have been trying for many years to stop the deprecations of the small group of dishonest promoters, who are detrimental to Canadians and Americans, but it has been difficult because they rarely come into the United States, knowing they will be clapped into jail the moment they do. We have secret indictments outstanding against a considerable number of these men, and they are wary. In the few cases where we found them in this country, we have arrested them, only to have them put up bail in amounts ranging as high as \$50,000 and then cross the border into Canada. We have been unable to secure their return for trial because so far as securities frauds are concerned, our present extradition arrangements with Canada are wholly inadequate and archaic.

Without the benefit of an adequate extradition treaty we have had to put other strings to our bow. We have turned evidence over to the Postmaster General of the United States and he has issued fraud orders requiring that any mail addressed to the named offenders be returned to the senders stamped "fraudulent." These orders have had some good effect, but as a practical matter there are so many points in the United States at which mail is made up for Canada, that it has been virtually impossible to effectuate these orders thoroughly with existing personnel.

Furthermore, the names were changed on the return envelopes and "Accounting Department" and "New Business Department" and post office box numbers in quick succession have been used, and it has been necessary for us to follow up with supplemental fraud orders.

Progress along the lines I have indicated herein could not have been made without the help of the legitimate securities men in Toronto and other parts of Canada.

Just a few months ago the Broker-Dealers Association of Ontario helped us considerably by ruling that any member of the Association -- and most broker-dealers in Ontario belong to the Association -- who used return envelopes bearing any other name or address than that carried on his registration with the Ontario Commission would be subject to disciplinary action. This is important not only because it will make our fraud orders more effective, but because it is indicative of a large area of understanding that has developed between us and Canadian officials. We now look at this problem as a joint problem of equal moment to both Canada and the United States. We can look forward to further cooperative actions between our countries for the general protection of the investor.

We have also resorted to publicity as the means of informing people about fraudulent operations. Newspapers and periodicals all over the country, Better Business Bureaus, Chambers of Commerce, and indeed the securities industry itself have advised people that a phone call or a three cent stamp may save them a lot of money. All of these factors -- fraud orders, publicity, and cooperative effort -- seem to have had a real effect which has become evident in recent months.

However gratifying these developments may be, we always have maintained that the necessary base upon which any permanent and reasonably complete cure can be built is revision of our extradition treaty with Canada. There is no doubt that such revision is required and without it we believe our whole enforcement program will lack any permanent foundation.

The laws of both Canada and the United States have kept pace with modern securities fraud techniques. Unfortunately, our treaty with Canada, entered into at the turn of the century, has not. It is necessary to bring the treaty up to date so that it reflects the broad criminal laws that both countries have passed to cover such situations. The treaty, like these criminal statutes, should reflect the common morality of our people. We at the Commission feel quite confident that, given such a treaty, we will have the requisite machinery to put teeth into the enforcement efforts of both Canada and the United States.

In the early 1940's, after we had tried unsuccessfully to obtain extradition for securities fraud under the present treaty, we made our initial effort to secure its revision. In 1942 a rather broad treaty covering both fraud and violation of registration requirements was agreed upon. The United States Senate ratified the treaty, but the objections raised to it in Canada were such that it never passed the Committee stage in Parliament. A similar effort at revision failed in 1945. The problem then became much more acute because of the pent-up demand for investment of accumulated savings. All this time the Commission has continued to press for negotiation of a new treaty. We narrowed our extradition aims to the simplest common denominator -- fraud and that alone. And we did a great deal of missionary work in an effort to convince the Canadians of our good will and high purpose. The result was that a few months ago the Prime Minister of Canada presented to the Parliament a resolution embodying a Supplemental Treaty which has been signed by the governments of the United States and Canada.

It is a very simple document. People who violate the fraud provisions of the Securities Act of the Mail Fraud Statute, or who violate similar Canadian laws, will be subject to extradition at the request of either country.

This treaty amendment will go into effect when it is ratified by our Senate and is approved by the Canadian Parliament. We do not foresee any difficulties on this score, and we are confident that obstacles that thwarted previous revision attempts will not be met this time.

Thus a problem of many years standing is well on the way to being resolved -- to the mutual benefit of both countries. The problem has been a most aggravating one to us. A gigantic confidence game -- and that is what it has been -- is a major irritation, even for a rich country like the United States. For Canada too this racket has been detrimental. This money should have gone into the development of the resources and industry of this half-continent. The fact that during the same period, the flow of American dollars to legitimate ventures in Canada greatly exceeded the take of the mail racketeers, proves only how vast are the possibilities for development of the great resources of Canada. We at the Securities and Exchange Commission hope that by helping to eliminate this obstacle we have removed a major impediment to complete mutual confidence, and we trust that the result will be a greater rather than a lesser volume of American investment in Canada.

Our Government has spent a great deal of money throughout the world in an effort to strengthen the free nations which are standing shoulder to shoulder with us, and to help develop their resources in the common defense. This has been an expensive policy, but I think it has been a necessary one, and I am proud of our leadership which is responsible for it. I also believe that it is infinitely more desirable, wherever possible, that such development take place through the use of private capital rather than by government funds. In the case of Canada, we have resources so vast and opportunities for commercial development so favorable that private capital needs little encouragement. Where we have such a situation it behooves us to remove any obstacles that may be in the way.

I am happy to state that this problem is on the way to a solution through the efforts of both our countries, and we can look for continued cooperation for the two aims we have in mind -- the development of the Canadian potential and the protection of the American investor.