

# NEWS

## SECURITIES AND EXCHANGE COMMISSION

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### LIFE BEGINS AT FORTY

An Address By

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Securities and Exchange Commission

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Mr. Chairman; Ladies and Gentlemen:

This is a time for remembrance for me. My inclination to reminisce could easily exceed your tolerance, and I do not intend to search the limits of the latter. But I cannot stand here this afternoon, having received this most gratifying honor, without being full of recollections of my brief but rewarding formal association with New York University Law School.

I came down here from Cambridge in July, 1950, as the direct result of the persuasive powers of then Dean Russell Niles. I had stayed on a fourth year at Harvard as a teaching fellow, participating in the development of its group work program for first year law students. Dean Niles was interested in a similar program here, and I therefore had an attraction to him for that purpose. Furthermore, he was offering the then generous salary of \$5,000 for the year, plus the opportunity to earn extras. With three small children, my wife and I could not afford to be indifferent to money.

We settled in the original Levittown, where some of my classmates were already living, and I made the acquaintance of the Long Island Railroad and commuting from Wantagh. To

help pay for the move, I was allowed to take over the second half of the summer night school course on civil procedure -- my half to be code pleading. Since that subject had produced my lowest mark as a student, the assignment was a challenging one such as only a hungry man with a hungry family would accept.

The course was scheduled for two nights a week in the old loft building around the corner. The older gentleman who had taught common law pleading for the first half of the summer, and who obviously had a strong distaste for such irresponsible innovations as code pleading and young squirts, introduced me to the class with that charming observation that you can always tell a Harvard man but you can't tell him much, and mercifully disappeared -- from my sight if not from my memory. Whereupon the class talked me into collapsing our two nightly sessions into one night a week for three hours.

So I began my formal teaching experience talking from seven to ten p.m. on sultry August nights on a subject that I had scarcely mastered, to 20 or 30 sleepy people, in a dreary room on the eighth floor of the old building with no air conditioning, and all the sounds and smells and soot blowing

in through the open window. It was not the best way to teach or learn the law, but it was an effective test of stamina, and it made what came afterwards comparatively easy.

My first regular course for the day students came in the fall, and the subject was contracts -- something I felt more comfortable with than procedure. Here I thought I could start some kids off right with the tough Socratic method. Our first case was Hawkins v. McGee, of loving memory to a generation of law students weaned on Professor Fuller's casebook, and I called on some poor, miserable soul toward the back of the large class to state the case. Naturally, everything he said was wrong and much of it foolish, which I made very clear to the class as I kept him nakedly exposed and suffering for half the period.

When it was over, I returned to my office in glowing satisfaction at such a fine beginning. Shortly afterwards, then Associate Dean Ralph Bischof invited me down to his office to discuss my first class and how it had gone. I gave him a glorious report which he listened to patiently and then said, "Ray, that first-year student has just left here

and won't be back. He just resigned, saying he didn't come here to be embarrassed and publicly insulted."

"Well, Dean," I said, "with such a thin skin he probably would never make it as a lawyer."

"Possibly," replied Ralph, "but Ray, he was a Phi Beta in Philosophy from Columbia and had a very high LSAT score. Please don't scare away all of our more promising students."

It's awful what young and inexperienced teachers can do. No one had really ever been that cruel to me, and I was ashamed. I have often wished since that that young man has found a rewarding life elsewhere and has been able to forgive me.

That was all in the old building. The next year we moved to the new. No one who did not live through the transition can quite appreciate the excitement it produced. It was far more than an improvement in physical comfort. It brought with it the promise of great things to come, and they have come. I left for the practice in Chicago the next year, so I didn't stay around to help very long, but the school has become everything that Arthur Vanderbilt,

Russell Niles, Mike deCapriles, Ralph Bischof, and the others dreamed of in those formative years, and I remain very proud of my association with the institution.

But this is not the only subject of reminiscences. Last Thursday evening, we celebrated the 40th anniversary of the founding of the Securities and Exchange Commission. The party was necessarily limited to present and past members, staff, and their spouses. Over 1,000 persons attended, including nearly 600 alumni and their wives and husbands. It was a grand affair and a striking demonstration of the depth of feeling engendered by service with the Commission.

The first of the Federal securities laws, the Securities Act of 1933, was initially administered by the Federal Trade Commission, which commenced operation in 1915. It was the next year, with the adoption of the Securities Exchange Act of 1934, that the SEC was created and vested with the administration of both acts. The organization was modeled generally on that of the FTC, with five commissioners serving five-year, staggered terms, with no more than three

of the same political party. The act says nothing about a chairman, but at its first formal meeting, on July 2, 1934, at 5:10 P.M., the only business transacted was to elect one of the five commissioners, Joseph P. Kennedy, as Chairman. In 1949, on the recommendation of the first Hoover Commission, the President was given the authority to designate the Chairman, but I am told that the change was more of form than substance, that the commissioners had always elected the chairman preferred by Presidents Roosevelt and Truman.

The agency was, of course, born of the miseries beginning with the great Stockmarket Crash of 1929, which was followed by the Great Depression. Economic historians have argued ever since whether the Crash was caused by those financial and economic factors that were leading toward the Depression, so that the Crash was but the first tangible evidence of what was to come, or whether the Crash caused the Depression, suggesting that, without the excesses and chicaneries of Wall Street, there would have been no Depression. Whatever the better interpretation might later appear to be, the two calamities were obviously closely associated in the minds and emotions of people in the early '30's.

What is more, the atmosphere was not one of calm repair of a faltering market mechanism. It was widely felt that Wall Street had betrayed America, that it was populated by crooks and thieves, and that they must be punished and thereafter controlled and forced to behave in the public interest. Those many investors who had been wiped out in the Crash were not just unhappy at their loss, they felt they had been cheated, and many of them, at least, were right in so feeling. Beyond that, if the stock market's failings can contribute to such widespread suffering as the Great Depression, then something must be done about it.

Considering the passions of the time, it seems remarkable, on reflection, that the legislative remedies were as mild and conservative as they were. While much more radical notions of government control and public ownership were gaining temporary ascendancy in other economic areas, the approach of Congress to our securities markets was not to impose government control over the flow of capital or the quality of investments, and certainly not to upset the ownership of American business by individuals, but rather to make the systems fairer and more responsive.



Full disclosure of facts about investments and the elimination of rigging and manipulation in the markets were the basic cures. Despite what was going on in those early days of the New Deal concerning agriculture, utilities, and all of industry in the abortive NRA, securities legislation was dominated by the spirit of Brandeis through Frankfurter to Landis, with ample borrowing from the British approach. The private ownership of, and trading in, corporate securities was to be preserved and, indeed, fostered by making investors better informed and the markets more fair and honest.

This is not to say that everyone on Wall Street or in corporate management recognized the Federal securities laws as friendly and as the least repressive alternative to something much worse. There was resistance and hostility. The Trade Commission had at least made a beginning at administering the Securities Act, governing the registration of corporate securities for public sale. Indeed, some of the fundamental features of that process -- the staff review of filings, the letter of comment, the delaying amendment and the red herring prospectus -- date from that first year. The staff that had begun that work at the FTC

under Baldwin B. Bane, moved over to the new SEC virtually intact. (For years at staff and alumni gatherings, when games got going on who really was the veteran, the person who could remember the days at the FTC was hopelessly one up on anyone else who couldn't. The last of those veterans' veterans retired in 1971.)

Baldy Bane, as he was known to everyone, was one of those remarkable figures in the Civil Service whose presence can hardly be planned, but who show up from time to time in critical places when needed. A Southern country boy with some years on the staff of the FTC, he had no pretensions to great scholarship or sophistication in financial matters, and was no match intellectually for those who drafted the law. But he had the practical good sense to develop procedures necessary to make the Securities Act work. As the Act reads, though sound in concept, it would scarcely have been effective without the Baldy Bane extra-statutory innovations.

There also came over to the SEC from the FTC, Judge Healy of Vermont, a tough Republican strict constructionist, who was to serve longer than anyone else to date, 12 years, as a commissioner.

So the new agency inherited the Securities Act in pretty good initial condition with competent staff to continue the work, but the Exchange Act was something else, brand new and requiring the imposition for the first time of Federal supervision of that citadel of Wall Street, the New York Stock Exchange. People respond variously to being told that Joseph P. Kennedy was the first chairman. He was a restless man who only stayed a year before leaving to head up the Maritime Commission, and he is reported to have observed that if the Exchange Act had been adopted 10 years earlier, he would never have become a millionaire. At any rate, I think he was a good choice to start things off, giving the Commission courage and practical knowledge when it very much needed it.

Once in being, during the first six years, the SEC collected other laws to administer that, at least in terms of legislative germination, are kindred. These are the Public Utility Holding Company Act -- imposing upon the Commission the enormous and unprecedented task of supervising the reorganization of most of the electric and gas utility

industries -- the Trust Indenture Act of 1939, certain duties under Chapter X of the Bankruptcy Act, the Investment Company Act of 1940, and the Investment Advisers Act of 1940.

From shortly after its adoption in 1935, until the early 1950's, the Holding Company Act was the Commission's principal business in terms of man hours. Until after World War II, the volume of industrial financing remained low. But these were nevertheless extremely fruitful and formative years in developing concepts, attitudes, procedures and relationships. In those years, the Commission and its staff were blessed with outstandingly able and public-spirited men whose work was collectively sound and good, but whose most important legacy may have been the spirit of high professional competence, personal honor, and practical judgment that characterize the SEC at its best.

I believe it is fair to say that the legal and administrative structures formed in the '30's served us well during the long post-World War II bull market until the crescendo of the '60's collapsed about five years ago. How has it worked in the bear market of the '70's? It is tempting to say that the system has worked, not to preserve securities values, which was never its purpose, but to preserve domestic

tranquility during a period of severe and widespread losses. Certainly the latter is an important aim of Federal securities regulation. If we are to preserve free capital markets, then prices are going to go down as well as up, and it is necessary that investors generally suffer down periods with a justified confidence that their losses result from market forces and not from crookedness and cheating, else people would not invest to begin with or would have revolutionary inclinations when they lost.

Our populace is by no means free, even today, from suspicions that the securities markets are rigged against them. Some of the mail I receive asserting these suspicions as certainties seems pathological, but by no means all of it. Nor can I be surprised that someone who has lost his savings in one of the spectacular failures we have witnessed in the last few years finds it hard to accept the proposition that American business is fairly, honestly and competently managed in the interest of all shareholders. But while these losses have resulted in individual tragedies, bitterness in some quarters, and an apparently widespread disinclination to return to our equity markets, they have not led to public uproar equalling that in the early '30's.

In candor, however, it must be noted that the decline in securities prices since 1969 has been severe but has not quite matched the dramatic plunge begun in October 1929. Furthermore, and probably of more significance, the decline in the stock market has not been accompanied by a general depression even approaching that of the early '30's. If the warnings of present and impending severe recession now being heard are well-grounded, and nothing happens to reverse the trend, we may have a different assessment to make.

But, even assuming that we are justified in regarding our system of regulation as successful in the limited sense I have just described, we nevertheless are in a process of re-evaluation, reassessment, and new beginnings.

In his recent autobiography, Mr. Justice William O. Douglas writes --

The great creative work of a federal agency must be done in the first decade of its existence if it is to be done at all. After that it is likely to become a prisoner of bureaucracy and of the inertia demanded by the Establishment of any respected agency. This is why I told FDR over and over again that every agency he created should be abolished in ten years.... Roosevelt would always roar with delight at the suggestion, and of course never did do anything about it.

Since we have now been around for four times our allotted span, and have in a sense presided over a full cycle of market activity, this idea raises some interesting questions. Should we swap the system and start all over with new concepts and a new agency? Are we so much the "prisoner of the bureaucracy and of the inertia demanded by the Establishment" that we should be recycled? We intend to prove the negative and in some respects are already proving it.

I am not sure just what Establishment Justice Douglas has in mind, but the most obvious possibility in relation to our work is not likely to agree that we are subject to inertia at its demand. Indeed, we are not at the moment terribly popular in many quarters of Wall Street today, and it's not likely that this is going to change much any time soon. While this seems to be a fact, it is not a source of pleasure. There is danger in the suggestion that the success of our agency, or any agency, should be measured directly by the extent of its unpopularity among those subject to its jurisdiction. This has political attraction from time to time, but our true mission is to avoid temptation to court either popularity or unpopularity and to be governed by what seems

best -- the public interest within the mandate given us by Congress and the wisdom given us by our Creator.

So we at the Commission are striving to shun worries about whether we are prisoners of bureaucracy, whatever that means -- if it means that the Commissioners are ruled by the career staff, we are not beyond the quality of their arguments, which is very high -- or whether the Establishment has immobilized us, We are concentrating on the tasks ahead, and they are formidable indeed.

While our basic mission, the creation and preservation of fair and efficient capital markets, has not changed, the role we must play to that end has. The simpler days when our capital markets were booming and we were primarily the cop on the beat to guard against excessive greed, are gone. Today we are faced with the task of participating in the reconstruction of a shattered system so that, when other economic forces once again make investments in corporate securities generally attractive and business is able to begin the large scale raising of the new capital it so urgently needs, the securities industry will be as strong and as efficient and as fair as possible.



This is not a simple task. The necessary technology is available but the regulatory problems involving, among other things, the accommodation of so many conflicting interests are complicated and sometimes baffling.

Along with this major program of developing, or causing to be developed, a modern central market system, are other problems, either new or assuming new dimensions. The role of commercial banks in the securities markets, once thought to have been put to rest in 1933 with the Glass-Steagall Act, has now become of major concern, in part because of the rapidly increased competition of our banks with foreign banks who suffer no comparable inhibitions.

The efforts of our government to work toward the free and open flow of capital among nations will also present us with new challenges. We must develop efficient facilities for stimulating this flow without relaxing unduly the disclosure and liability protections to which American investors are entitled. Somewhat related to this is the growing concern for knowledge of who owns American businesses. Our domestic devices for hiding stock ownership are pretty good but they are primitive compared to those available in foreign countries.

And we must be deeply concerned with restoring to investors the confidence that they do in fact have available to them complete and meaningful information regarding their investments. This includes primarily financial information but other matters as well.

Whatever may be true of other agencies with other jurisdictions, it often seems today that the work of the SEC has just begun. Is it worth the effort? Is the notion that capital is allocated best by the free decisions of individual investors, fully informed, naive, or at least unobtainable? Is it impossible to provide and maintain securities markets so fair and efficient that they will be attractive repositories for savings? Can we, indeed, ever succeed in instilling and preserving in Americans general confidence in our present system for the ownership and management of the means of production and distribution?

We are confident that it can be done and that we can help do it. That is the job before us for the next forty years.