THE SECURITIES ACT OF 1933
AND ITS APPLICATION TO MINING SECURITIES

Address

of

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of the

Securities and Exchange Commission

before the

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I am very glad to be able to accept your invitation to come to this convention and discuss with you some of our problems, your problems and ours. I appreciate the privilege and I appreciate also the responsibility that privilege imposes.

In the short time allotted it would of course be impossible to discuss even briefly all of the provisions of the Securities Act of 1933 which relate to the financing of mining companies. I know, however, that you, or at least many of you, are particularly interested in the registration provisions of the Act and in the exemption rules where registration is not required. Some, perhaps many of you have heard these provisions and exemption rules discussed at other meetings and conventions, by me or by some other representative of the Commission, but since they directly affect your business, and since to some the rules are still not altogether clear, perhaps further discussion will be of some help.

You probably know that, primarily, the general purpose of the Securities Act of 1933 is to secure a full and fair disclosure to the investing public of the facts regarding securities offered for sale. If registration is effected, this information becomes available through the registration statement itself and from a prospectus filed with the registration statement. The prospectus must be given to the investor at or before the time the security is offered for sale.

To effect the purpose of securing a full and fair disclosure, the Act requires that when a new issue of securities is to be offered for sale to the public and unless some exemption is available, a registration statement must be filed with the Securities and Exchange Commission. If the registration statement appears to comply with the provisions of the Act and the rules, it becomes automatically effective twenty days after it is filed in Washington, D. C. During those twenty days, experts connected with the Registration Division of the Securities and Exchange Commission examine the statement and if it is found to be sufficient, no action is taken by the Commission and the registration becomes effective and sales may be made. If, on the other hand, the statement appears to contain untrue or incomplete information or is inaccurate in any material way, the registrant is notified of the deficiencies and then has the opportunity to file amendments. Until necessary amendments are filed, sales are not authorized.

When a statement becomes effective sales may be made. No certificate, no permit, is required. The Commission can not and does not "approve" a security. Were the Commission to approve a security it would justify the inference that an agency of the Government was recommending the security to the prospective buyer as a safe investment. That is a responsibility, you will appreciate, the Government can not assume. So though the statement becomes effective, that fact does not indicate nor can it be represented that the Commission has either approved or disapproved or passed upon the merits of the security, nor can it be regarded as assuring the truth or accuracy of the disclosures made in the statement. The obligation to tell the truth is placed upon the issuer and if the statement contains false representations, the issuer and those who sign the statement become subject to the civil and criminal sanctions provided by the Act.

Under the civil provisions of the Act if the information given in the registration statement is false, or misleading, then those responsible for the false or misleading statements must return to the one who has been

misled, the money he has paid for the security. Those responsible for the false or misleading statements would also have to defend a fraud complaint, should one be filed.

And may I assure you that it isn't intended nor has it been the practice of the Commission to place any serious obstacle in the way of legitimate business. Even speculative securities, if legitimate, may still be offered and the public is as free as ever to buy them. The Act is meant in no way to substitute the judgment of the Government for that of the individual investor as to the wisdom or advisability of making any investment. He must be told truthfully what is back of the investment. The decision then rests with him.

Because of restrictions in the Federal Constitution, the scope of the Act is limited to the regulation of sales of securities made through use of the mails or by means or instruments of transportation or communication in interstate commerce.

By the provisions of the Act itself and by the Rules and Regulations adopted under it, many exemptions from registration requirements are made available but I shall direct my comments to those exemptions which, from the experience we have had, we find are the ones most often claimed by issuers of mining securities. First is the exemption under Section 3 (a) (11), sometimes referred to as the intrastate exemption. From the number of violations which have occurred with respect to this exemption, it is apparent that its scope is not well understood by the issuers who seek to avail themselves of it. Yet if the provisions of the exemption are carefully read, there should be no difficulty in understanding its requirements. The exemption is available to "any security which is part of an issue sold only to persons resident within a single state or territory where the issuer of the security is a person resident and doing business within, or, if a corporation, incorporated by and doing business within such state or territory." This means that if, for example, a corporation be incorporated in the State of Montana and transacts business in the State of Montana and offers its securities only to legal residents of the State of Montana, it is not necessary to file a registration statement. The amount of the offering makes no difference.

Regarding the scope of this exemption, Mr. Allen E. Throop, General Counsel of the Securities and Exchange Commission, said in a public release issued May 29, 1937: "The legislative history of the Securities Act clearly shows that this exemption was designed to apply only to local financing of such a nature that it may practically be consummated in its entirety within the single state in which the issuer is both incorporated and doing business. Accordingly, this exemption is so worded as to be available only to a security which is a part of an issue sold only to persons resident within the state in question. In any consideration of the exemption, it is essential to appreciate that its application is thus expressly limited to cases in which the entire issue of securities is offered and sold exclusively to residents of the state in question.

"Moreover, since the exemption is designed to cover only those security distributions which, as a whole, are essentially local in character, it is clear that the phrase "sold only to persons resident" as used in Section 3 (a) (11) cannot refer *merely* to the initial sales by the issuing corporation to its underwriters, or even the subsequent resales by the underwriters to distributing dealers. To give effect to the fundamental purpose of the

exemption, it is necessary to take the view expressed by the Federal Trade Commission during its administration of the Securities Act, that if the exemption is to be available, 'it is clearly required that the securities at the time of completion of ultimate distribution shall be found only in the hands of investors resident within the state.' Any such sales to non-residents, *however few*, and even though legal in themselves, would preclude compliance with the conditions of Section 3 (a) (11), and would render the exemption unavailable.

"The so-called 'intrastate exemption' is not in any way dependent upon absence of use of the mails or instruments of transportation or communication in interstate commerce in the distribution. If the residence of the purchasers, the residence or place of incorporation of the issuer, and the place in which the issuer does business are all confined to a single state, the securities are exempt from the operation of Section 5 of the Act. Securities thus exempt may, without registration, be offered and sold through the mails, may be made the subject of general newspaper advertisement (provided the advertisement is appropriately limited to indicate that offers to purchase are solicited only from, and sales will be made only to, residents of the particular state involved), and may be delivered in interstate commerce to the purchasers."

Another exemption many of you have heard of is the one provided for by Rule 200. This is the exemption many times referred to as the "$30,000 exemption." The rule, which establishes this exemption, provides that any offering of securities is exempted from registration if the aggregate offering price to the public does not "exceed the sum of $30,000; it also provides that the amount of the offering shall be reduced by the amount of any other offerings (whether public or private), within one year prior to the offering exempted, of securities of the same issuer, or of any person controlling, controlled by, or under common control with such issuer, unless, or except to the extent that, such offerings have been withdrawn."

The $30,000 rule is designed to enable a mining corporation or any other issuer to secure a small amount of capital without the necessity of filing a registration statement. But, as stated, the rule requires that the aggregate offering price to the public of the securities for which the exemption is claimed shall not exceed the sum of $30,000. And the General Counsel for the Commission has expressed the opinion that this rule implicitly requires that the entire present program of financing the company involved shall not exceed the $30,000 limit permitted and an issuer may not obtain an exemption under this rule if the amount presently to be offered forms in substance a part of a substantially larger issue to be marketed in the near future. To illustrate, a scheme that contemplates the organization of a corporation with a capital say of $90,000, and the disposal of the entire $90,000 at the rate of $30,000 per year would be in violation of the provisions of this rule.

From the $30,000, too, as has been said, must be deducted the amount of any securities offered to the public within the year unless the offering has been withdrawn, and there must be deducted also any securities transferred in all private transactions during the year prior to the date of the offering. In the mining industry, private offerings or sales would include stock exchanged for machinery, equipment, promotion, wages, leases, property, etc. All such transactions occurring within the year must be considered and the stock involved be deducted from the $30,000. The rule also provides that if the issuer is controlled by or under common control with another issuer or

other issuers, the aggregate offering of all can not exceed $30,000.

A third exemption applicable to the sale of mining securities is provided by Rule 202. If the provisions of the rule are complied with and the offering does not exceed a total price to the public of $100,000, the exemption is available. Under the rule, the security may be sold for more but it must not be sold for less than its par value, or, if no par stock is involved, it must be sold for not less than its stated value; the amount of $100,000 must be reduced by the amount of any other offerings of securities of the same issuer which, within one year of the offering for which the exemption is being claimed, were exempted from registration solely by reason of this or any other exemption rule, unless, or except to the extent that, such other offerings have been withdrawn; also the net proceeds, after deducting all sales expenses, shall be not less than 75 per cent of the aggregate amount paid by the public for the security; certain types of promotion stock can not be sold during the period of distribution. This promotion stock must be placed in escrow so that it can not be sold until the issuer shall have earned a net profit from operations for a period of one year; or until the purchaser for cash has received back 75 per cent of the amount he paid; also a prospectus containing the information called for in the rule must be prepared and filed with the Securities and Exchange Commission before it is used and a copy of the prospectus must be given to each purchaser at or before the time the stock is offered to him.

Contrary to an impression which is rather general, to prepare this prospectus is not at all difficult. No complicated details are required. Answers must be given to only 13 questions. These answers will disclose, among other things, the names and addresses of the corporation officers, the description of the properties, the number of shares issued to its promoters for services and the number exchanged for its property, the amount of its debts, funded and current, and if annual salaries of more than $6,000 are to be paid, the names of those who are to receive such salaries must be given.

A fourth exemption applicable to mining securities is the exemption provided by Rule 210 recently adopted by the Commission as a trial exemption and available for use until October 29th, 1938, when the time may or may not be extended. Rule 210 exempts all offerings up to $100,000 provided the offeror complies with the laws of each state or territory to whose residents the securities are offered. Under the exemption provided by this rule no security shall be offered, sold or delivered after sale except in compliance with all state or territorial laws relating to the regulation, qualification and licensing of securities and dealers which are applicable to the transaction of offering, sale and delivery after sale or which would be applicable if such transaction were effected within such state or territory to whose residents the securities are offered for sale. The rule further provides that no offering shall be made under the rule until the issuer shall have filed with the Commission, at Washington, D. C., a letter of notification containing the following information: "(A) the name and address of the issuer and of each principal underwriter; (B) the title of the issue, the amount proposed to be offered, and the proposed offering price per unit and aggregate offering price of the securities proposed to be offered; (C) a list of the States and Territories in which it is proposed to offer the securities; and (D) the title of issue of all securities of the issuer previously sold or subscribed for pursuant to an

offering under Regulation A commenced within one year prior to the commencement of the proposed offering, indicating the aggregate sale or subscription price of such securities. No offering shall be made under the exemption provided by this rule in any State or Territory which was not listed in the original letter of notification until the issuer shall have filed a supplementary letter stating the name of such additional State or Territory.

"There shall be inserted in a conspicuous part of any written communication prepared or authorized by the issuer (or by a person controlling, controlled by, or under common control with, the issuer) offering for sale any security herein exempted, in type as large as that used in the body thereof, the following statement:

> 'These securities have not been registered with the Securities and Exchange Commission because such securities are believed to be exempted from registration. But such exemption, if available, in no sense indicates approval by the Commission of the merits of these securities.'

"However, the above statement need not be included in any communication (A) which merely states from whom a written prospectus may be obtained and, in addition, does no more than identify the security, state the price thereof, and state by whom orders will be executed, or (B) which is made to a person who concurrently receives, or previously has received, a written communication relating to the same securities and containing such required statement.

"Ten copies of each written communication prepared or authorized by the issuer (or by a person controlling, controlled by, or under common control with the issuer) which is proposed to be used at the commencement of the public offering, or intended to be sent or delivered thereafter to more than ten persons, shall be filed with the Commission in Washington, D. C., prior to any use thereof.

"No security of the issuer shall be currently offered under the exemption provided by Rule 200, 201, 202, 203, or 206."

A short time ago clarifying amendments were added to the Rule 200, 202 and 210 exemptions which we have just discussed. The amendments read as follows: "The aggregate offering price of assessable shares of stock shall be taken as the sum of the offering price thereof determined as hereinbefore provided, and the aggregate amount of all assessments which may legally be levied thereon."

This amendment affects the offering of any company whether it sells stock or gives it away, and has the intention to levy assessments to secure its cash capital. Under these rules, no exemption is available for issuers of assessable stock unless the total amount of assessments which may be levied is limited to the amount the rule exempts. The Commission has stated that the amendments do not involve any change in policy, but are intended merely to clarify the scope of the exemptions.

Sometimes we hear it said that there are some who have the impression that the Commission looks with disfavor on mining securities. Nothing could be farther from the truth. The problem of any industry such as mining which produces around one and one quarter billions worth of raw materials per annum and which ranks with agriculture as a basic industry are problems which we

realize deserve careful and sympathetic study. But in that industry and its financing there exists an element of speculation which, with the possible exception of oils, is not found in any other field and that very fact has been seized upon by unscrupulous promoters who use it dishonestly to further their schemes. The pocket book of the public rather than property is mined. Promises mean nothing to this ilk. They are absolutely devoid of conscience. There is a pot of gold at the end of every rainbow. The credulity and the need of old men and old women, the widow and the orphan, is criminally imposed upon; they are lied to; cheated and robbed. It is of vital concern to you to recognize that the very nature of your industry makes it possible for men of no conscience to bring discredit upon it. From these unscrupulous ones every one suffers. Money is directed away from legitimate investment and legitimate speculation which should be encouraged, into the pockets of those whose only concern is to get all they can and keep out of jail.

It may surprise and interest you to learn that beginning with the year 1919 and continuing up to 1931, more than $50,000,000,000 in securities were issued in the United States and sold to the public, and of this 50 billion, approximately 20 billion were worthless or nearly so. A vast sum of money diverted away from legitimate business; enough to pay more than one half of our national debt, huge though that debt be, and gone into the pockets of those whose concern for the welfare of the industry is absolutely nil.

Any action of the Commission which has the effect of discouraging such promoters should, and I believe, does receive the approbation and commendation of a group such as yours. It must, therefore, seem that the need for adequate disclosure of information increases in importance as the speculative boundaries of the enterprise are widened. Losses are never easy to take, losses are sure to occur, but losses resulting from deception are within control. To the extent that those losses can be removed, both industry and the investor are served. The problem is not ours alone, it is yours. That we may assist in solving the problem is our earnest desire. And that its solution is of greater importance to your industry than any of us realize is our sincere belief.

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