Address of James M. Landis before the National Association of State Security Commissioners at New Orleans, Louisiana, November 12, 1934.

It has been my privilege hitherto to have addressed only audiences composed of those whose activities have been placed under the jurisdiction of our Commission. It has been my good fortune to have escaped unharmed from these audiences but not always unscathed. This afternoon, however, it is a different group to which I have the privilege of talking -- an audience of government rather than of business, of men clothed with a duty of assuring a fairer deal to our investing public rather than of men for whom such an end is merely a desire, indeed, an audience that may fairly be called the trustee rather than the beneficiary of security regulation. For it is in terms such as these that I think of legislation governing our security exchanges and the sale of securities, in terms of benefit rather than repression, in terms of regulation that redounds not only to the advantage of the individual investor but also to the advantage of the originators and sellers of securities.

It is now some five months since the Securities Exchange Act of 1934 was passed, but only a little more than one month since it has been in active operation. The causes of its origin are well known to all of you, causes that it is wise not to forget so that we may remain firm in our resolve that the record of the last decade shall not again be repeated. The opposition that the Act engendered during its passage through Congress, and that broke fruitlessly against the stern insistence of a President, a Congress and a Nation -- an insistence in no uncertain terms that our security exchanges are so deeply affected with a vital public interest that they must be controlled in the interest of the large public that they serve -- this opposition is now gradually disappearing. Much that was once said of the Act and its main purposes now proves itself to be untrue, and the legislation as well as its administration, I trust, is beginning to demonstrate itself as furthering its primary objective of making our security exchanges function both more honestly and more effectively to meet the financial needs of our economic society.

In trying to sketch for you some of the activities of the Securities and Exchange Commission since its organization in July of this year, let me at the same time remind you of some of the larger objectives of the Act. The first is that of seeing to it that our stock exchanges shall be places for open and honest dealing, that their rules shall be fair and equitable, and that certain practices which have been permitted in the past shall be definitely abandoned. To effect these ends the Act required all stock exchanges either to be registered or, if their volume was small in character, to be specifically exempted. All the large exchanges and most of the smaller exchanges applied for registration. It was granted to them upon the condition that they require by rule that any violation of the Act should be disciplined as well as penalties imposed upon any conduct of a member that was contrary to just

and equitable principles of trade." A question, however, was raised with reference to one exchange, the New York Mining Exchange, and after a hearing that brought forth evidence reflecting seriously upon its conduct and organization, it withdrew its application for registration and retired from business. All the smaller exchanges requesting exemption were granted a temporary exemption for sixty days, pending investigation and hearing as to whether the exemption should be permanently granted and if so upon what terms. Officials of the Commission are now engaged in conducting investigations into these exchanges and hearings are being held with reference to them throughout the country from Boston to Los Angeles.

In the interest of fair dealing on exchanges The Act also bans certain practices by making them unlawful and in numerous other cases authorizes the Commission to prescribe regulations governing other aspects of doing business on exchanges. The Commission thus has two functions, of investigation upon complaint or otherwise of violations of the Act in this respect, and of study to formulate rules to govern the other matters entrusted to its jurisdiction. It has already conducted a number of investigations in order to determine whether market manipulation in the form of pools, jiggles, wash sales or the like was taking place. It is also conducting investigations preparatory to the formulation of rules and regulations governing such matters as short selling, puts and calls, pegging and stabilizing operations, the use of stop loss orders and numerous other similar matters. One of its large exploratory tasks is that of making a general examination of the activities of floor traders and of specialists in order to determine how it can wisely carry out the statutory mandate to restrict their dealings so far as practicable to those necessary to the maintenance of a fair and orderly market.

This aspect of the Commission's work is varied and extensive. It requires the aid of men versed in stock market practices to watch these markets daily and to act as trouble-shooters when any justifiable suspicion of unfair conduct appears. It also requires a group of men to study scientifically the operation of our security markets in a way that has yet to be done. The economic merits of many of these questions are still a matter of debate so that ways of retaining that which is good and eliminating that which is economically evil have yet to be devised. Moreover, the gradual overhauling of the rules of our many exchanges in order to insure fair dealing to the extent that rules can do so, will take thought and study, but out of these we may expect in time exchanges more fairly and more efficiently organized.

I turn now to where lies, perhaps, the greatest of all tasks that faces the Commission. This is the development of adequate corporate reports from the issuers whose securities are listed on exchanges. It is a commonplace of our thought that we, more than any other country, are a nation of security holders. Our large corporations possess literally tens of thousands of stockholders, whose stockholdings though they be small are of equally great significance as those of the large stockholders. Consequently, management more than ever owes a duty to disclose adequate and in revealing form the record of its stewardship. The unfortunate market practices which have occurred during the past decade flourished, in the main, only because of the atmosphere of ignorance that

enshrouded corporate activity. Had the full truth been told by management, and had management devoted its attention to management and not to market manipulation, the record of the past decade would have been vastly different.

It would be idle for us to pretend that corporate reports in the past have been always truthful and revealing. There are, of course, outstanding exceptions in this field, but too often accounting practices have been employed for the purposes of concealing rather than of revealing the true situation to the investing public. Then again much of the concealment has been due to a certain secretiveness on the part of corporation executives based upon the theory that only their competitors would benefit from such disclosures as might be made by informative financial statement. Hardly fifty per cent of the listed corporations on the New York Exchange, I am told, reveal anything more about the operating success of their companies than to give a general figure of net operating income. Though, of course, in instances there may be validity in this claim for privacy, there can be no doubt that in the majority of cases the idea cannot be seriously entertained that to give a fair and full report of corporate assets and profits will give an unfair advantage to competitors. Certainly, except in unusual instances, where such a claim is insisted upon, one may well doubt the desirability of encouraging or permitting public investment in the enterprise.

Without adequate corporate disclosures the basis of stable investment is, of course, lacking. If the figure given as earnings in an income statement represents other than true earnings or includes without disclosure a non-recurring profit, the uselessness of estimating market value in terms of a ratio to earnings is only too apparent. And market values accurately to reflect the conditions of corporate success to corporate failure rather than of mere market activity must bear some relationship to earnings.

The Securities Act of 1933 and the Securities Exchange Act of 1934 give the Commission a great opportunity to deal with this problem so as to evolve standards of corporate reporting that shall be both adequate and consistent. Much has already been done by some of the larger exchanges towards requiring more effective disclosures. But in significant instances these exchanges with the best of intentions have failed. They need and have needed the strong arm of government to assist their efforts. For, in addition to depriving the resisting corporations of the exchange market, some other disability must necessarily attach to those corporations who refuse without good reason to meet the minimum standards of full and fair disclosure.

The Securities Exchange Act, following the general principle of the listing requirements of the exchanges, requires as a condition precedent to registration on an exchange the disclosure of specified financial and other information. It also empowers the Commission to insist upon periodic reports as a condition to the continuance of those privileges which registration upon an exchange gives. When the Act first came into operation, it was necessary for the Commission, in order not to disrupt the

continuity of business on the exchanges, to accord to all securities then listed on exchanges, as well as to specified classes of securities admitted to unlisted trading privileges, the right of temporary registration. But this right expires under the law on July first of next year. By that time a permanent system of registration will be in force, and standards for the adequate reporting of financial data prescribed. The Commission is now at work on these forms and hopes to have them before the public within a short time. The task has been a difficult one, to evolve standards that will at the same time reveal the facts and not mean an unnecessary and expensive burden for corporations. It is, of course, too much to expect that one can overnight attain the ideals of corporate reporting that we hope eventually to reach. Accounting is not yet, and can, perhaps, never be, an exact science. Indeed, I am tempted to believe that on occasions we have sought too strenuously to use the dollar and cents measuring rod to gauge matters which are intrinsically incapable of being subjected to that type of measurement. But the Act and the Commission's powers are here to stay, and by a wise exercise of these powers over a period of years we may hopefully seek to build up the type of adequate and informative corporate records that will make for more stable values and a greater tendency for investment as distinguished from speculation.

Two other aspects of the Securities Exchange Act are related to this problem of corporate reporting. The first of these seeks to again apply this principle of adequate and truthful disclosure to the solicitation of proxies. If we are to revive our faith in the older idea of the corporation as a business entity which sought to give its stockholders the right by virtue of their investment to participate in the policies of management, we must succeed in dealing with this problem. The way in which stockholders have been induced to ratify particular management policies without even a disclosure of what these policies are, is well known to almost every holder of a voting security. Stockholders' conduct in the large has been unintelligent in its appraisal of management. It could not be otherwise so long as stockholders were kept in ignorance of what management was seeking permission to do. Means must be found not only to bring about a disclosure of what stockholders are asked to vote upon, but to simplify corporate problems for judgment by them, if their rights under the existing conception of a corporation are to be enjoyed.

The second of these related aspects of the Securities Exchange Act is that section which deals with transactions by officers and directors and large stockholders in the stock of their corporations. It is aimed at preventing these insiders from profiting at the expense of the large body of stockholders who can never hope to possess an amount of information equal to that which those at the helm of the corporation are bound in the ordinary course of events to acquire. But the function of these directors and officers is to manage and direct their corporations and not to speculate in its securities. To effect that end the Act requires monthly reports of changes in their holdings to be made to the exchanges and to the Commission. It also requires profits made upon a quick turnover of stocks in these corporations to be returned to the corporation itself and not held for the private benefit of the directors and officers.

I have not time today to deal with those aspects of the Securities Exchange Act which concern the excessive use of credit for speculative purposes, or, in other words, margins and borrowing by brokers and dealers. The control of these avenues and uses of credit was entrusted to the Federal Reserve Board. Their margin regulations went into effect upon the fifteenth of October, and a margin ratio was prescribed, in accordance with the statutory standard, that is neither deflationary nor unduly restrictive.

But there is one aspect of the Securities Exchange Act that I particularly desire to mention. This concerns the control given to the Commission of over-the-counter securities and over-the-counter markets. Very broad powers, extending even to the point of requiring the registration of brokers and dealers, were granted to the Commission over these matters. The grant had two purposes in mind. One was to prevent listed corporations from seeking these markets in order to evade the duties of disclosure that continuance upon the exchanges would have imposed upon them. But more important than this was the purpose to do something with the over-the-counter markets themselves. Practices exist on these markets, as you well know, comparable in every degree from the standpoint of economic undesirability with those that once prevailed upon the exchanges. Indeed, on the less respectable over-the-counter markets practices which could not have been indulged in even on the least respectable of our stock exchanges, still persist. Moreover, as regards the majority of securities dealt with on these markets, neither adequate initial nor periodic corporate reporting is to be found. Some means for dealing with these defects is required.

Here, more than anywhere else, lies a field for cooperative effort between the federal and the state governments. Adequate surveillance of these markets cannot be accomplished by the federal government alone, for their supervision would require a veritable army of men. Much has already been done by the states through direct suppression of frauds and by effective registration of brokers and dealers. But the interstate aspects of these markets have on occasion made them unamenable to state control, and much security distribution these days of the undesirable kind has sought the shelter of interstate commerce. We have already uncovered several large schemes of the sell and switch type that employed the long distance telephone to reach customers across state lines. But more that sporadic enforcement is demanded in order to cope effectively with this problem. A well-planned attack is needed that will employ the available resources of both the federal and the state governments as well as the cooperation of the investment banking fraternity. What the lines of this attack shall be are matters to which we have already devoted much attention. One of its features calls for the establishment of regional branches of the Commission in New England, the Atlantic States, the South, the Southwest, the Middle West, the Rocky Mountain Region and the Pacific Coast. We must be within ready reach not only of the various exchanges, but also of the sources of the origination of the many types of securities and the centers wherein these securities are distributed. Our strength must be present not only for itself but also to aid and buttress the states in our common objective to eliminate unfair and unethical practices in these markets.

It has been difficult in this short time to picture to you the details of the Act which we are called upon to administer. And to sketch except in a very brief way our activities since our organization, would take too long. Indeed, it seems to me that I have lived a lifetime since last July. And to crowd that lifetime into a short half hour is impossible. But I hope that at least I have given you some sense of the ends that we are pursuing, of the small progress that we have made, in which we have built wherever possible upon the experience of the states, and of the pioneer country that is still before us. With the objectives of legislation such as this, none of us (whether regulators or regulated) can find true fault. In its sphere it seeks purposes essentially akin to those that state security legislation has long sought and in part attained for itself. And if one purpose of your annual assemblage is not merely to increase your wisdom in dealing with your problems, but also by the sense of communion to increase your resolve to meet the challenge of your duties, may I hope that in bidding you "God Speed" in your efforts, some echo of those words will find its way back to us to cheer us in our task.

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