

OFFICIAL REPORT OF PROCEEDINGS  
BEFORE THE  
SECURITIES AND EXCHANGE COMMISSION

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DOCKET No. ....

In the matter of-- THE PROBLEM OF MAINTAINING ARM'S-LENGTH  
BARGAINING AND COMPETITIVE CONDITIONS in  
THE SALE AND DISTRIBUTION OF SECURITIES of  
REGISTERED PUBLIC UTILITY HOLDING COMPANIES  
AND THEIR SUBSIDIARIES.

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Place ..... Washington, D. C.

Date ..... January 27, 1941

Pages ..... 1 to 206

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SECURITIES DEALERS, INC.  
821 - FIFTEENTH STREET  
WASHINGTON, D. C.

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BEFORE THE  
SECURITIES AND EXCHANGE COMMISSION

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Public Conference concerning  
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THE PROBLEM OF MAINTAINING ARM'S-LENGTH  
BARGAINING AND COMPETITIVE CONDITIONS  
:
  
in  
THE SALE AND DISTRIBUTION OF SECURITIES  
:
  
of  
REGISTERED PUBLIC UTILITY HOLDING  
COMPANIES AND THEIR SUBSIDIARIES  
:
  
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----- X

Hearing Room 1102,  
Securities and Exchange Commis-  
sion Building,  
Washington, D. C.,  
Monday, January 27, 1941.

Met, pursuant to notice at 10:30 o'clock a.m.

PARTICIPANTS

COMMISSION:

- JEROME N. FRANK, Chairman, (Presiding)
- SUMNER T. PIKE, Commissioner
- ROBERT E. HEALY, Commissioner
- EDWARD E. ERCHER, Commissioner

STAFF OF COMMISSION:

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- ROBERT H. O'BRIEN, Associate Director, Public Utilities  
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## P R O C E E D I N G S

Chairman Frank: I am sorry that the limitations of space have prevented us from doing what we intended to do.

We wanted this to be a very informal conference, and we had intended to sit down on the floor instead of assuming this dignified posture. But you just pretend that we are down there, and have our feet on the table, and you can unbutton your vest, and put your feet on the table and talk in the freest possible fashion.

The purpose of this conference as you know, is to discuss competitive bidding for utility securities. The idea is by no means new or radical. Competitive bidding for utility securities has, for many years, been required by several states -- in conservative old New England. It is required by the Federal Power Commission and the Commission for the District of Columbia. We are here today to discuss whether it should be extended and applied by us to utility securities under the Public Utility Holding Company Act of 1935.

The Commission's purpose -- to use the statutory language -- is to protect the interest of investors and consumers and the public interest in public utility holding company systems. The Commission has no purpose or desire to hurt investment bankers or dealers. We want to find out whether competitive bidding for utility securities will hurt

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anyone, and, if so, whom.

Before we proceed to the discussion, there is need for some clarification. We are, I repeat, to consider with you today a rule, proposed by our staff, requiring competitive bidding for utility securities. The rule would apply only to securities of public utility holding companies, registered under the Public Utility Holding Company Act of 1935, and their subsidiaries. The proposed rule has nothing whatever to do with any other securities of any other kinds of companies. The Commission has not the slightest statutory power to require competitive bidding as to such other securities. And it is not seeking any such power from Congress.

Some persons, unfortunately, confuse the Securities Act of 1933 and the Public Utility Holding Company Act of 1935. Let me briefly differentiate: The Securities Act covers the securities of all kinds of companies, including utility companies. But it gives us very limited powers. Speaking generally, it calls merely for telling the truth about, and dealing honestly in, securities. The Utilities Act of 1935 overlaps the Securities Act of 1933 with respect to certain utility securities. As to such utility securities, it gives the Commission much broader powers and duties, than does the Securities Act of 1933.

The subject for discussion today divides into two



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major parts, which we shall hear separately:

First, has the Commission the legal -- that is, the statutory -- authority to make a rule, under the Public Utility Holding Company Act, as to competitive bidding for utility securities?

Second, if the SEC has such statutory power, is it desirable -- in the public interest or in the interest of investors or consumers -- to exercise that power?

The Commission has not yet reached a conclusion on either of those points. Before it does so, it wants to hear discussion from you today and to consider the memos which have been filed with it on that subject.

The Commission has never in its history acted on any subject when it considered that it lacked statutory authority. Nor will it do so in this instance. If after considering the arguments, the Commission decides that a competitive bidding rule as to utility securities is outside its powers, it will certainly not issue such a rule.

Some of you -- perhaps many of you -- who are present today have never conferred with us before. All of you are not intimately acquainted with our habits. And we fear that you may have been misled, by certain published statements, as to what has happened with respect to our earlier discussions of competitive bidding. It is therefore, desirable to acquaint you with the facts.

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The uninformed person might think from the statements of certain persons that we are proposing to act precipitately with respect to a competitive bidding rule. That is an unjustified innuendo. Here is the story:

As you know, for several years, the subject has been much discussed by leading investment bankers. Harriman Ripley and Morgan, Stanley, over a year ago, published booklets discussing it.

The participation of the SEC in this discussion began about a year ago, in this fashion:

In 1938, while Mr. Justice Douglas was Chairman of the SEC-- and Commissioners Healy, Mathews and I were members-- we adopted a rule, under the Utility Act of 1935, as to the sale of utility securities through affiliated investment bankers. In practice, that rule led to considerable criticism by the investment bankers. Suggestions for changing it were made.

In an opinion of the Commission, in December 1939, in a case dealing with that rule, Commissioners Eicher and Henderson suggested a substitute rule requiring competitive bidding for utility securities.

On February 7, 1940, Mr. Connely, President of the IBA, called on me to discuss it. I told him that we were then contemplating sending out a questionnaire asking for comments on our rule about affiliated bankers, and that that question-

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naire would call for views on the subject of requiring competitive bidding for utility securities.

The next day, February 8, 1940, Mr. Connely wrote me a letter. It reads as follows:

"INVESTMENT BANKERS ASSOCIATION OF AMERICA

"New York, N. Y.

"February 8, 1940

"Honorable Jerome N. Frank,  
Chairman, Securities and Exchange Commission  
Washington, D. C.

"My dear Chairman:

"I have been thinking about our conversation of yesterday and the thoughts that I am about to express here might have developed had we had a little longer time to talk over the subject to 'Compulsory Competitive Bidding.'  
of [?]

"If I understood you correctly it was your idea to send out a questionnaire listing certain questions which would be answered by not only people in our business but by industrialists, etc.

"This idea has a lot of merit providing the questionnaire is sent to an informed group and by that I mean people who have some understanding of this business.

"If you send this questionnaire out to a broad mailing list it will include a lot of manufacturers or small business men who have never done any public financing and you are

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likely to get an entirely different reaction than if you confined your mailing to members of the IBA, the NASD and such industrial and public utility concerns which have registered with the SEC during the past five or six years. At first blush when you mention competitive bidding to an uninformed person their reaction is bound to be that it is a desirable thing. However, I know from actual experience that when you begin to discuss the pros and cons of the case it is not unusual for an uninformed person to change his viewpoint after you have given him the reasons why compulsory competitive bidding for industry is not desirable.

"Now I say all this knowing very well that as laws now exist the Commission could only force compulsory competitive bidding under the Holding Company Act. In utter candor I must say that if the Commission should decide to force compulsory competitive bidding under the Holding Company Act it might be just another step to amend the Securities Acts and make it compulsory for private concerns to use the sealed-bid route.

"I remember very well your idea about classifying securities, ranging from AAA to the speculative type and I would like to think a little more about this.

"I was pleased to learn that in any event you had no thought of 'freezing' the matter until you send out the questionnaire, compile the results, draw up some tentative

conclusions as a result of the questionnaire and then discuss the matter with those of us in the business.

"Have I stated my understanding correctly? This is a very vital subject and I want to be sure that we understand each other.

"With kind personal regards, I am

"Sincerely yours,

E. F. Connely,

President."

You will note the following about that letter from Mr. Connely, written on February 8, 1940 -- almost a year ago:

He said that there was "a lot of merit" in our contemplated proposal to send out a questionnaire on the subject.

He questioned the advisability of sending it out except to "an informed group and by that I mean people who have some understanding of this business." He thought we should confine our mailing "to members of the IBA, the NASD and such industrial and public utility concerns which have registered with the SEC during the past five or six years."

He was pleased that we would not adopt a rule until we should "send out the questionnaire, compile the results, draw up some tentative conclusions as a result of the questionnaire, and then discuss the matter with those of us

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in the business."

You will observe that he did not suggest a public hearing or public discussion, but wanted us to have a limited "discussion" with a restricted group.

On February 29, 1940 -- some three weeks after the receipt of Mr. Connely's letter -- we sent out the questionnaire to public utility companies, investment bankers, public utility commissions and others, asking for replies by March 20, 1940. On March 13, 1940 we extended the time for replies until April 2, 1940.

On March 18, 1940 -- ten months ago -- Mr. Connely for the IBA, filed a lengthy reply to the questionnaire. It discussed, at length, competitive bidding for utility securities.

This reply was very widely publicized in the press of the country. We understand that copies were then sent by Mr. Connely to all members of the IBA.

On April 2, 1940, we received a lengthy reply from NASD, which also discussed competitive bidding for utility securities. We understand that this reply -- or a summary of it -- was sent out to all the members of NASD.

Many replies were received by us, to our questionnaire, from other persons -- investment bankers, utility executives and others.

So it appears that many, many months ago, it was widely

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publicized that the SEC was considering a rule, requiring competitive bidding for utility securities; and that proposal, at the express request of the SEC, was publicly and widely discussed many, many months ago.

On May 17, 1940, the members of this Commission conferred on the subject with a committee from the NASD. We told that committee -- and at about the same time, told IBA representatives -- that we would study the numerous replies to our questionnaire and that we would again discuss the question with them and others interested before we adopted any such rule.

We recently learned that the IBA, last May 1940, sent out a questionnaire to its members asking their views on competitive bidding for utility securities.

From May to December, 1940, the Commission's staff and the members of the Commission have had much correspondence on the subject, and numerous conferences with investment bankers, dealers and others.

On December 18, 1940, we sent out, for comment, the staff's report dealing with that subject. In large part, it is a discussion of the points made by the IBA, the NASD and others in memos received by us in March and April 1940, in response to our questionnaire of February 29, 1940. We then announced that we would be glad to have round table discussions of that report with interested persons.

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That was scarcely precipitate action.

We originally asked that written comments on the December 18, report be sent to us by January 6, 1941. But on December 23, 1940, IBA and NASD asked for further time, and we then extended the time for written comments to January 20, 1941. And we then set today, January 27, 1941, for this public conference.

This was a little over one month from the date when we sent out the staff's report -- and about 10 months from the time when IBA sent us, and widely published, on March 18, 1940, its lengthy comments on competitive bidding for utility securities.



We submit that, on that record, there have been no precipitate moves, no undue haste, on our part.

I turn now to another notion which has recently been widely publicized and which should be dispelled before we proceed with the discussion:

Under date of January 18, 1941, Mr. Connely, filed with us the lengthy comments of the IBA on the staff's report. In his transmittal letter, Mr. Connely makes this statement:

"In an endeavor to work on a cooperative basis with the Commission and to solve our problems in a manner approved by the public and the Congress, during the past several months our representatives and those of other interested elements have, from time to time, been engaged in discussions with members of the Commission's Legal Staff and of its Trading & Exchange and Registrations Divisions.

"While these discussions did not specifically encompass the Public Utility Act of 1935, it was our understanding that the conferences would deal with all problems arising under the 1933 and 1934 Acts or having to do with the regulation of the exchanges or the regulation of underwriters and dealers."

We are not quite sure what Mr. Connely meant by that statement. If he meant to say that the Commission has in some way violated an express or implied understanding relating to amendments affecting the Utility Holding Company Act, then it must be said that the Commission never heard of such an

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understanding until nine days ago. It has never breached any understanding made by it. Any suggestion that there was such an understanding on that subject is entirely unjustified, if that is what was meant by the statement. In order that those here present may see that that is so, let me recite the pertinent facts:

You will recall that on March 18, 1940, we received from the IBA its reply -- and in April 1940, the NASD reply -- to our questionnaire of February 29, 1940, discussing, at length, competitive bidding for utility securities, and that we then advised them both that we would continue to study the matter and advise them before we adopted any rule on the subject under the Public Utility Holding Company Act. Keep those dates in mind -- March and April 1940.

Not long after, on May 20, 1940, the Commission received, from Congressman Lea, Chairman of the House Committee on Interstate and Foreign Commerce, a request for comments on a Bill then pending; and on June 10, 1940, received a similar request as to another pending Bill.

Those Bills related solely and exclusively to amendments to the Securities Act of 1933; they did not relate in any way to the Public Utility Holding Company Act, or any action which might be taken thereunder, as to competitive bidding or otherwise.

Those letters, and a proposed Congressional committee

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hearing on those Bills, were discussed with representatives of the IBA and the NASD and others.

As a result of those conferences, and with the concurrence of the conferees, the Commission, on June 17, 1940, wrote Chairman Lea that we would confer with the IBA and NASD and others, during the balance of the year, concerning amendments to the Securities Act and the Securities Exchange Act; and we suggested that consideration by Congress of any amendments to those Acts be postponed until January 1941, to permit of such conferences and the making of a report on the subject.

At that very time, the IBA and the NASD knew full well that we still had under consideration a rule, under the Public Utility Holding Company Act, as to competitive bidding for utility securities. But that letter of June 17, 1940, to Chairman Lea, written with their knowledge and concurrence, made no mention of that subject or of the Public Utility Holding Company Act.

On June 18, 1940, Chairman Lea graciously replied, in a letter to us, stating that our proposal was satisfactory, and that he was therefore, "with the approval of the industries affected," cancelling hearings on the pending Bills which had been set for June 19, 1940.

On June 19, 1940, Mr. Connely, on behalf of the IBA, wrote Congressman Lea and the SEC letters expressing concurrence in the views set forth in our letter of June 17.

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He said nothing whatsoever about amendments to the Public Utility Holding Company Act or any action which the Commission might take thereunder with respect to competitive bidding for utility securities or otherwise.

Similar concurrence was expressed about that time by NASD. Again there was no reference to the Public Utility Holding Company Act.

I am filing, with the stenographer, copies of the letters to and from Chairman Lea, Mr. Connely and the Commission.

Conferences between the SEC staff and the IBA, NASD and others, concerning amendments to the Securities Act and the Securities Exchange Act, have been in progress since September 1940. They are still going on. I am delighted to say that all concerned believe and have said that substantial progress has been made.

Now it is important to note that, in those conferences, no mention was made by anyone of competitive bidding for utility or any other securities under any statute, including the Public Utility Holding Company Act, or of any other matter relating to that Act. The sole subject matter was amendments to the Securities Act and the Securities Exchange Act.

While those conferences were going on we sent out, on December 18, 1940, as I have said, our staff's report on competitive bidding for utility securities under the Holding Company Act, for study and requested comments.

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Nine days after that report on competitive bidding for utility securities was thus sent out for comment -- on December 28, 1940 ; with the full concurrence of the representatives of the IBA (including Mr. Connely) and the NASD, we wrote Chairman Lea, asking for further time, until the latter part of February 1941, to complete our conferences concerning, and our report to Congress on, proposed amendments to the Securities Act and the Securities Exchange Act. No one on behalf of IBA or NASD or anyone else suggested to us that that letter should refer -- and it did not refer -- to competitive bidding under the Holding Company Act or to any other matter relating to that Act. Yet at that time Mr. Connely knew as well as he knows now that we are considering whether or not to adopt such a rule under the Public Utility Holding Company Act.

Subsequently, on January 6, 1941 -- three weeks ago -- representatives of the IBA and NASD conferred with the members of the Commission. They then urged that no action be taken on the competitive bidding rule under the Public Utility Act until the Securities Act was amended. They specifically were asked by the Commission whether their request was based upon any alleged understanding that the conferences then going on, with reference to amendments to the Securities Act and the Securities Exchange Act, were to include action taken under the Public Utility Holding Company Act. Their

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reply was "no".

They put their request solely on a legal ground, namely, that, because (they said) of provisions of the Securities Act of 1933, any rule under the Public Utility Holding Company Act with respect to competitive bidding might be unworkable, and that, therefore, amendments to the Securities Act were necessary in order to make workable any rule on competitive bidding for utility securities under the Public Utility Holding Company Act. The Commission was not convinced by that legal argument. It pointed out to them, that, if that legal argument were sound, then it was impossible to explain how it was that many millions of dollars of utility bonds had been sold since 1933, under the competitive bidding requirements of several states, by prominent investment banking houses -- which are members of the IBA -- without encountering any such difficulties under the Securities Act of 1933 as it now stands without amendments.

And so, down to and including January 6, 1941 -- three weeks ago, the record is this: It was clear that no one said and no one indicated that he thought, or could reasonably have thought, that there was any understanding, express or implied, that the subject of a competitive bidding rule as to utility securities under the Public Utility Holding Company Act of 1935 was to be included in the agreed conferences with the IBA and others relating to amendments to

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the Securities Act of 1933 and the Securities Act of 1934, and in the report to Congress on such amendments.

In the light of these facts, we were astonished when for the first time, nine days ago, in Mr. Connely's letter of January 18, 1941, it was suggested that there had been such an "understanding" between us and the IBA.

So much by way of clearing the atmosphere of suggestions of precipitate action or bad faith on the part of the Commission.

We desire to have this conference informal but orderly. We shall try to conduct the discussion by topics. But we will not be rigid in our conduct of the conference.

We shall first hear comments as to the wisdom or unwisdom of the proposed rule, assuming, during that part of the discussion that we have the statutory power to make it. Later in the day, we shall call for comments on our statutory power to make it. [Later in the day, we shall call for *omit?* comments on our statutory powers.]

First, however, it will be helpful if the staff reports on certain suggestions for modifications of its proposed rule, recently received, which the staff regards with some favor.

Is the staff ready with that comment?

Mr. Weiner: Yes, Mr. Chairman.

Chairman Frank: Just before you proceed, it is necessary

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for Commissioner Pike to attend for a time another conference. I hope you will be back as soon as possible.

I want to say that I know that you will value his views. I speak for myself. I certainly do. He is a person, who has had, before he came on the Commission, much the same experience that you gentlemen have had, in connection with the purchase and marketing of securities, and his reaction to the discussions and the memorandums which we will receive, I consider of considerable value.

Mr. Stewart: Mr. Chairman, before the staff begins to put their ideas forward, I would like to clear the atmosphere, as to whether or not there has been a breach of the understanding.

There has not, in our judgement been any breach of the understanding with respect to the amendments of either the 1933 or 1934 Acts. We had no intention of conveying that idea to you. If it has been conveyed, we wish to clear it up now.

Chairman Frank: Very well, just forget what I said.

Mr. Stewart: But we do believe that the problems under the 1933 and 1934 Acts are inseparably interwoven. That we hope to convince you, as time goes on.

Chairman Frank: We had a discussion on that subject but that wasn't the end of it, and when we come to the



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legal discussion, we will be glad to hear what you have to say.

I am glad to know there has been no suggestion of any breach, and my remarks on the subject can therefore be forgotten.

Mr. Weiner: A number of suggestions with respect to individual portions of the rule, which were not commented on in our report, and it occurred to me that it might be well to bring those suggestions forward now, so that others will have an opportunity to submit whatever they may desire to say regarding them.

Perhaps the simplest way would be to proceed in the order as set forth in the rule itself, which is printed at pages 45 to 46 on the Staff Report. So far as --

Chairman Frank: (Interposing) What pages did you say?

Mr. Weiner: Forty-five and forty-six. So far as the major principle involved in the rule of course, that was commented on at great length and I had no thought of calling any attention specifically to any of those remarks.

So far as variants of the proposed rule itself are concerned, the following might be brought forth so that they can be commented on later.

The first exception on page forty-six now reads as follows:

The issuance or sale of any security pro-rata

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to existing holders of securities of the applicant or declarant. There, the several points have been brought to our attention.

In the first place, it is noted that the term securities, would include any type of security, and that read literally, that exception would permit going to the present holders of bonds and offering an exchange solely to them.

It has been suggested that that would be undesirable that it would be contrary to the spirit of the general rule and ought not to be permitted.

We think there is a good deal of merit in that suggestion.

A further point to which attention has been called, is that the language of that exception as now drawn might present some difficulty in those cases where the offering to existing security holders is coupled with a stand-by agreement or some other form of underwriting.

After studying the rule, we recognize that there would be some difficulty in the rule as drawn, and we think that that situation should be clarified.

A third point that has been made in connection with that exception, is that it is said to be too restrictive. For example, in a reorganization, the offering might be made not to the security holders of the one company, but to the security holders of another company in the same sys-

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tem, in some form, either of section 11, reorganization, or liquidation. I think we would probably all agree that such offerings could not feasibly be made competitive as that was c contrary to the object of the rule.

Our present thought is that that situations are very easily recognized and that exemption could, and would, readily be afforded under the fifth sub-division, which within its broad sweep was intended to embrace that kind of situation.

It has been suggested that the Commission might well announce a policy about it; if that should be necessary or desirable, it could be done.

On the second exception, broadly speaking, we have three suggestions.

One was to eliminate the word "unsecured".

That second exception deals generally with what might be called the Commercial Loan. However, because of the time period involved, namely up to ten years, it would include within its present sweep, what might and generally has been called intermediate credit.

The point made is that there is no sound basis for differentiation between an unsecured and a secured loan in that connection, the particular point being made that the bank might desire collateral and that the fact that collateral was given would not change the character of the loan, or the principal involved with respect to competitive bidding.

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The second suggestion to which I would like to call attention is the elimination of the present limitation that such loans must be made with a commercial bank.

That comes from the insurance companies, who feel that they ought to be permitted to participate in such loans on the same basis as a commercial bank.

The third suggestion coming from several sources is that the period is too long, and a shorter period has been suggested.

One specific suggestion was not more than three years. Other suggestions either were not specific, or had a different period of time.

It seems to us that all those suggestions are in one sense inter-related and we are inclined to see considerable merit in all of them.

I anticipate that some of those, who made the suggestions will be here and comment on them more fully.

I wanted to be sure that ever one was aware of it, and would therefore have an opportunity to make any appropriate comments.

On the next sub-division, there is a comment as well. That sub-division deals with the exemption of sales as to which the aggregate proceeds will not exceed a million dollars.

It has been suggested that that figure might well be

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raised to \$2,000,000.

We are inclined to think that there is merit in that suggestion and that it ought to be given serious consideration.

There have been one or two other points that perhaps might be clarified. We had one suggestion to the effect that to make the rule applicable to sales of portfolio securities, of non-utility companies, was stretching the commission's authority with respect to those sales.

I think it should be made clear that the rule was not intended to apply to such sales.

As the rule is drafted, it applies only in those cases where a declaration or an application for the sale is needed. In that case no declaration or application is required and therefore the rule would, by its terms, be inapplicable.

Perhaps that language isn't sufficiently clear. We thought it was, but if it isn't, it can be clarified if those interested in that exception would point out what they regard as the ambiguity, which led them to construe it otherwise.

There have been other minor suggestions, but I doubt whether it would be worth while to bring them forward here.

Chairman Frank: As to the manner or the order of presentation Mr. Stewart of the IBA has made two suggestions that seem perfectly appropriate to the Commission, unless someone has objection.

bz24

First, that those persons of the so-called smaller dealers be given an opportunity to speak first.

Second, that we treat the matter, so far as possible under several topics rather than to have each person speak ex-tenso.

We don't want to hold you rigidly to that, and if you find it awkward, why, we will depart from it.

We would, however, like to make this request.

There are a great many people here. We would like, if you can, to conserve our time, if you will state your views pithily if possible, and avoid too much repetition of what has been said by any predecessor.

If there isn't any objection, we will follow substantially Mr. Stewart's suggestion, and his first suggestion is that we take up as a first topic a consideration of the probable effect of competitive bidding on the position of the smaller dealers who seldom act as underwriters, but who ordinarily participate in selling groups formed to distribute corporate securities.

If anybody wants to respond --

Mr. Connely: (Interposing) Mr. Chairman

Chairman Frank: Mr. Connely.

STATEMENT OF EMMETT F. CONNELLY

President, Investment Bankers Association of America

Would it be in order if I made just a short statement

bz25

prior to that.

I am Emmet F. Connely, President of the First Michigan Corporation of Detroit, and President of the Investment Bankers Association of America.

It is in the latter capacity that I appear, although what I have to say I concur in the first capacity with. In order to conserve everybody's time, I will just read this rather brief statement.

As you can see, the decision before you is regarded so seriously by those of us who are involved one way or another, that I am supported by able witnesses from our business who represent all parts of the country. There are others present, who represent a fair cross-section of interests which would be directly affected by the proposed rule. These men have taken the time and trouble to come to give you the benefit of their practical knowledge and experience, and they will be very glad to give you just as much of that as time permits.

I do want to say however that we earnestly desire to discuss this matter in the manner that Chairman Frank has outlined, in a calm, dispassionate manner, in trying to arrive at what the right answer is.

A reading of the document of the Public Utility Division Staff and the IBA document indicates that there is a wide divergence of opinion.

I don't believe that in any way precludes the type of

bz26

discussion that both the Commission and we would like to have.

A question as serious as this, must be viewed and decided from the broad base of public interest.

The drastic changes that you are considering involve more than the interests of the investor or the investment banker, or the public utility companies.

It strikes at the very vitals of our system of security distribution and directly or indirectly reaches into every niche of our national economy. So, I urge that we be sure we are right and make haste slowly, for the arguments against competitive bidding in our opinion are cogent and timely.

From the view point of public interest, may one not raise the question as to whether or not it is wrong now to take the time of able men in all walks of life for this sort of a discussion when all energies, both within and without the government might better be devoted to the forwarding of the National Defense Program.

The President has said, and the country is in entire agreement with him, that no greater need exists today than to clear away all that slows down the defense program, and that we must remove the bottle-necks that now exist, and create no new ones.

One of the fundamental requisites of the Defense Program is the abundance and availability of dependable



power, chiefly electric power.

No industrial process, whether in the making of the machine, making of machine tools, or the fabricating of complicated parts and completed parts can be conducted without the use of power.

Most of the power available for national use comes from the electric light and power industry, which has been privately financed to the extent of Twelve billion dollars.

The National Defense program requires not only that no impediment be placed in the way of expansion of these capacities, but that such impediments as are in the way, be removed.

It is of paramount importance in our opinion that the well-known and accredited methods of private financing in this country should continue to function with every facility possible, so that capital needs for expansion in industry may be met without delay.

The engineer, whenever he wants to set up a plant that will function without question under pressure, uses only proved and tested apparatus, leaving for those who are not so dependent on results to experiment with what is new.

The present managements of business of the country and the accredited methods for opening the financial gateways for the free flow of private capital into these industries should be left, in this time of emergency, undisturbed, in order that maximum results may be produced with the maximum

bz28 of speed.

The time for experiments is not during a period of national emergency.

In passing the Holding Company Act of 1935, the objectives of Congress were not dissimilar to those which motivated it in passing the Securities Acts of 1933 and 1934, for the pre amble of the Holding Company Act states the purpose in the light of which the Act is to be interpreted as being primarily to protect consumers, investors and the public interest. ✓

So far as this Act is concerned, both investors in, and issuers of, securities are, in all reasonable respects, protected under the full disclosure theory of the 1933 Act.

And this includes prices and spreads for security issues.

Therefore, the need of an additional regulatory rule does not seem either necessary, or desirable at this time.

I would like to make the suggestion, in all frankness, for the good-will of the Commission, that along the lines that Chairman Frank stated that no conclusions had been drawn, that if it were possible, the SEC make available a complete monograph of all of the answers to the Commission's letter of February 29, 1940, on the U-12F-2 rule, as well as the replies received to date to the letter of the Public Utility

bz29

division's staff dated December 18, 1940 on compulsory, competitive bidding, and make this complete monograph available to all people in business, the public, and more particularly to the Congress, which body may ultimately have to settle this question.

Before stopping, I would just like to say one thing, to clarify in the minds of the Commission and the staff, what might be termed as criticism on our part, that we are down here today, instead of maybe 2 or 3 weeks from now.

There is certainly no criticism of the staff or the Commission on that point when you stop to think, take the line of reasoning that everybody has been familiar with this for quite a long time, but when you really do get a document such as Mr. Weiner's staff has put a tremendous amount of work on, and you get it at Christmas holidays no matter how much you know about the subject, you must read this.

I got this report, one of the first ones out, but it reached my desk about Christmas eve, and a couple days later, I came down with the flu.

I don't think there was any relation between the two things at all, but anyway, on my back, I had a chance to read it.

Chairman Frank: Ineffective competition of the proper corpuscles in your body.

Mr. Connely: Anyway, I had ten days to read this

bz30

thing.

Now a lot of my people didn't have the flu.

A lot of people didn't get this until actually we sent it to them.

We didn't think they were properly informed until they had read this, and also until they read our IBA document, and that was all we were pleading with.

I had a very good conversation with both Summer Pike and Judge Healy on the subject and I tried to make that clear.

I realized we ought to know all the answers, but honestly I don't think we had all the time we might have had for the particular study I am referring to.

In accordance with your suggestion Mr. Chairman, Mr. Stewart would be glad to pick up that first point with the smaller dealer, and ask some of them, or you may, whichever way you want to do it.

He has got a list of them.

Chairman Frank: I would like to suggest that as each person rises, he give his name to the stenographer, together with the name of his firm and, since this is informal, it may be desirable if someone makes a statement and someone else disagrees to allow questions or interruptions as time went on.

We'll see how that works out, but that may be the best way in the end.

dk1

Mr. Stewart: Thank you, Mr. Chairman.

Before we begin on the subject, I would like to add a word or two, if I may, to what Mr. Connely has said on the subject of haste.

We do not quarrel in the slightest degree with your dates but we do find that competitive bidding has been under consideration for a long time.

The <sup>Clayton</sup> Leighton Act was passed in 1914 and specifically mentions competitive bidding, but we have felt that, at this time, we are addressing ourselves particularly to a set of suggestions put forward by the staff, and we think that the facts about the discussions which took place prior to the appearance of that document have no direct bearing upon that document.

Certainly, they did not make it any easier to study or digest the document in order to prepare a reply to it.

We are sorry if we have overstressed the point, but let me say, from my own experience, that it was a very difficult task to go through it and to attempt to write a reply to it in the time made available to us.

Mr. Connely says he got the flu. I can vouch for that, because we kept him up until three o'clock in the morning. He helped us in getting the reply ready. He broke himself down to that extent.

We don't think we have been unreasonable in asking that

dk2

more time be made available for the study of this document.

Chairman Frank: I got a touch of flu without being affected by the report.

Mr. Stewart: The first subject on the agenda, Mr. Chairman, if agreeable to you, is the suggestion -- or, rather, the consideration -- of the probable effect of competitive bidding on the position of the smaller dealers who seldom act as underwriters, but who participate in the selling groups.

There are several representatives of the smaller dealers here.

As we have, I think, explained in the brief which we filed with you, it is our view that the requirement of compulsory competitive bidding would operate to the injury of the smaller dealers throughout the country, and by injuring them, would do injury to investors and to the general operation of our economic system.

Among the dealers who are here is Mr. Harold Emerson of H. L. Emerson & Company, Cleveland. We will ask Mr. Emerson to make a statement.

#### STATEMENT OF H. L. EMERSON

Representing H. L. Emerson & Company, Cleveland.

Mr. Emerson: I represent H. L. Emerson & Company of Cleveland, Ohio.

H. L. Emerson & Company was organized in 1933. We classify ourselves as a small dealer firm, which feels itself

dk3

not justified in taking a liability that attaches to an underwriting commitment.

Consequently our business is entirely one of distributing securities, at least 90 per cent of which are sold to investors and institutions in Ohio.

Our interest in the present discussion is vital, because we feel that the eventual result of the sale of new issues by corporations, through competitive bidding, will be to put us out of the business of distributing such new issues.

Before any distributor can adequately work on a new issue he must be sure of two things -- a firm supply of bonds and an adequate profit.

Today's selling group profits of approximately 3/4 per cent are small enough and already tend to force the selling group member to sell his bonds to professional and experienced buyers rather than placing them with a large list of buyers. In other words even now the conscientious dealer can not afford to spend time on the small buyer who really needs help and advice.

Competitive bidding we are convinced, instead of helping will further hurt this situation for two reasons. First, we believe that bidding procedure will follow that now prevalent with municipal issues, where a strong group buys the issues and distributes it with little or no help from a selling group. Second, obviously dealers spreads will be so narrowed that they

dk4 will be only a fraction of those now available.

Under present conditions municipal issues are offered with such a small selling commission that it is our practice never to work on them because we can not afford to go to the expense necessary to get orders and run the risk of not getting the order or being unable to fill it.

The small dealer will be a fundamental part of the investment and distributing business as long as the investment business remains a personal service business. Anything that tends to limit his activities not only is unfair to him but will deprive many of his small buyers of the value of his advice.

Actually better results for the country as a whole could be obtained by increasing rather than decreasing distributors profits.

Chairman Frank: Thank you, sir.

Mr. Stewart: Mr. Lowry Sw<sup>e</sup>ney of Lowry Sw<sup>e</sup>ney, Inc.,  
Columbus, Ohio.

#### STATEMENT OF LOWRY SW<sup>e</sup>NEY

Representing Lowry Sw<sup>e</sup>ney, Inc., Columbus, Ohio.

Mr. Sw<sup>e</sup>ney: My name is Lowry Sw<sup>e</sup>ney. I am president of Lowry Sw<sup>e</sup>ney, Incorporated, of Columbus, Ohio, a security distributing house, dealing in a generally diversified line of market securities, bonds and stocks.

We are fairly active in municipals and territorial issues but the bulk of our business lies in the corporation field,



dk5

where we participate actively in the various national issues, sometimes as an underwriter, but mostly on a selling group basis.

Operating mostly as a dealer and but little as a broker, we distribute our securities over most of the State of Ohio to banks, insurance companies, and other institutions and private investors.

I started in the securities business after my discharge from the Army in 1919, as a salesman for a New York underwriting firm; leaving them shortly afterwards, however, I went in business in the middle west and have had the position of a midwestern dealer for the last twenty years.

In discussing as fundamental a problem as that of compulsory competitive bidding on corporation securities, with all of its widespread ramifications, I feel that I had better stick to my last, as it were, and look at the question from the standpoint of the small dealer -- how will he be affected by it, and, even further, what will be the effect, if any, on the communities which he serves.

It would seem that thereupon is posed at once another question: Of what importance is this small dealer, anyway, in the scheme of things?

What is his place and value in the body economic, and what difference will it make to anybody, except himself, how he will be affected by competitive bidding, or anything else, for

dk6

that matter?

I realize, of course, that there is no statute on the books--at least, that I know of--that enjoins the Commission directly to underwrite or concern itself with the small dealer.

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However, I believe that, indirectly, his position is an important one, through his influence and necessity and his contacts with the individual investor and the public with whom the Commission is concerned. I dare say it is easily understandable that I might be somewhat prejudiced in favor of the small dealer. Many people feel, as I do not, that necessity is laid upon him of justifying his existence in a utilitarian society that yields no pensions or parasitic income. Be that as it may, I think the small dealer can easily pass all tests with flying colors.

I will not try to go too far afield and digress at a hearing of this kind to rehearse the more or less familiar arguments of the value of the small dealer to his community--his circle of friends and clients--whose financial or investment problems steadily circle around him as their center.

These arguments are familiar to every member of the Commission, but the point is that small as these problems may seem, set in a <sup>national</sup> rational frame, they are all important to the people involved, people whose numbers multiplied by small dealers throughout the land may run into many millions.

ar6

I say you cannot remove the small dealer without considering the alternative -- a return to the chain store system of security distribution of the 20's, a few large New York houses with 57 varieties of offices scattered all over the country with concentration and centralization of power in a few hands.

This should not occur again, particularly I would think at this time above all others should we do everything we can to avoid tampering with that mechanism whereby the investment requirements of our land reach out and tap the fundamental source of our national credit; the savings of the individual investor.

Chairman Frank: I think it is fair to say that this Commission has not heretofore been credited with the desire to increase concentration and control.

Mr. Sweney: I think that is perfectly true.

Chairman Frank: I think also it is true--I think the representatives of the N.A.S.D. can tell you that the Commission in its conferences with the N.A.S.D. has shown an ardent desire to protect the small dealer and to see that he, within the limits of the law and the obligations and duties of this Commission under its several statutes, has a real place in the sun.

Your remarks, therefore, appeal to the people that have had those sentiments continuously.

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Mr. Sweeney: Thank you, sir.

Mr. Stewart: I think, Mr. Chairman, that the small dealers generally were somewhat shocked by the statement in the Staff report at page 33 that the problems of the small dealer were not within the province of that study.

Mr. Healy: You have misquoted the report.

Mr. Stewart: In what respect?

Mr. Healy: You left out the word "general." This report, of course, does not deal with the general problem of the small dealers. It does deal with the problem of the dealer in relation to this problem. If you will look back at an earlier page you will find the statement included that the Staff has the point in view that the competitive bidding rule may work out to the benefit and advantage of the small dealer.

Mr. Stewart: That is right, Judge. I think that what we are concerned with here is most definitely the general problem of the small dealer.

Chairman Frank: I don't think that the Commission needs any defense on the subject of its interest in the small dealer. Our public utterances, speeches made by members of this Commission on numerous occasions, our constant concern through the N.A.S.D., the very creation of the N.A.S.D. through the Maloney Act, which was fathered by this Commission, has always had an intense interest in the small dealer.

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We believe that the large dealer can pretty well take care of himself. We do know that the small dealer needs help and, as I say, within the allowable limits of our statutory powers and duties which may call upon us to do certain things which the small dealer might not like us to do (I think often they are to his advantage although he doesn't know it).

We intend to do what we can to see that the small dealer has, as I say, his place in the sun. Nothing in the Staff's report was intended to indicate the contrary.

It did not intend to indicate the contrary; in fact, as Judge Healy has pointed out, it went out of its way to express concern for the small dealer and indicate that the small dealer was being benefited. I may say it is somewhat humorous to hear the large dealers expressing, where the I.B.A. represents the large dealer and the N.A.S.D. represents the large as well as the small, shedding crocodile tears over an alleged interpretation of some words in our report taken by them inaccurately to indicate that we have no concern for the small dealer.

Mr. Stewart: The small dealers, Mr. Chairman, speak for themselves, and I think they are doing so.

Chairman Frank: They are doing so very effectively.

Mr. Sweeney: Of course, Mr. Chairman, I am a small dealer.

ar9

Chairman Frank: Yes, sir.

Mr. Sweney: Very small. And I might say that in casting around trying to find some different tack to bolster up the case of the small dealer, I hit upon the following point which I continue.

It is well recognized now by economists that in time of great National efforts such as lie ahead, the channeling into productive enterprise of public savings is a vastly different thing from spending borrowed funds.

In this view our own Treasury concurring, as witness their announced desire that forthcoming Government issues go to the ultimate investor rather than to banks. One is sound--the investment for the country's use of the country's savings--the other definitely inflationary through the creation of artificial deposit credit. Who can do this job as well as the small dealer?

This is a job right down his alley, and in these uncertain days when not brave but only foolish men venture to say what lies ahead, let us keep the small dealer at his post.

I firmly believe that the proposed rule requiring compulsory competitive bidding upon public utility securities will greatly hurt the best type of small dealer through a reduction and perhaps an elimination of an important source of his income.

I believe that in these days of lean earnings, it might

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even put some out of business. I say this because I believe it will seriously hamper, if not entirely prevent the formation of successful and profitable selling groups through the medium of which the average small dealer participates in National offerings. Only very rarely does one participate as an underwriter for amounts under \$100,000, but the great percentage of the thousand or so dealers, or selling groups, are from ten to fifty bond houses.

I believe that the profits of these houses from their selling groups' connections, built up by many of them by years of honorable effort, will shrink or disappear entirely for the following reasons:

First, Purchase groups under competitive bidding may increase in size or they may not, as compared to present underwriting:

Among these factors that might contribute to an increase would be a desire to augment the underwriting capital in the deal, particularly if it were planned to dispense with the selling group.

This might add to the number of medium--say, one-hundred-thousand-dollar members--but could not help the hundreds--500 to 1,000--of 10 to 50 bond selling group firms. On the other hand, purchase groups might decrease in size due to physical difficulties of price discussion, powers of attorney, and the necessity for secrecy, etc., between a large number

arily of firms, geographically separated. The meager statistical evidence available rather supports this, and underwriting might well become more and more concentrated. In any event there would still be only a few leading as now.

Competitive bidding would only result in a turnover of accounts.

Chairman Frank: May I ask you-- It may not directly bear on what we are discussing here, but it may--Is there in Ohio enough money to finance Ohio's public utilities? I have heard it said that the export of capital is one of Ohio's principal business.

Mr. Sweney: It would be my judgment that under present market conditions, that is probably not true. The market, as it is today, is of such levels that a very substantial amount of any Ohio utility financing will be sold outside of the state.

Chairman Frank: Must be sold?

Mr. Sweney: I say that exists today. That is due to the condition of our investing market. This has nothing to do with with spreads. If spreads under competitive bidding were increased, it might not help the small dealer, as there is no guaranty that he would get any of the increase.

Chairman Frank: Do you think-- this is a question, may I say, that the Commission put to representatives of the N.A.S.D. last May, and we never received an answer, although



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I understand we were to receive one.

Do you think it would be desirable for the Commission, assuming it had the legal power so to do, under the Public Utility Holding Company Act, to do something as to division of the spread between the initiating underwriter and the small dealer?

Mr. Sweney: No, I do not.

Chairman Frank: You do not?

Mr. Sweney: No.

Chairman Frank: I gathered that you thought that the amount was too small that the small dealer got. Would you mind repeating the statement that you just read?

Mr. Sweney: No, I say here that if under competitive bidding, spreads were increased--if they were increased--that it might not help the small dealer, as there is no guarantee that he will get any of the increase. If, on the other hand, spreads were decreased, as the proponents of competitive bidding claim, it might well follow that the small selling group dealer would be the entire sufferer.

The underwriters still make their former spread through the elimination of the selling group. Statistics available support this argument showing on competitive bidding deals, a much higher percentage of the spread being retained by underwriters.

Chairman Frank: Well, you do not think that if the

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Commission had the power in those circumstances, it would be desirable for it to exercise it to see to it that there was a fair apportionment between the underwriter and the small dealer.

Mr. Sweeney: I think, sir, from a practical standpoint you would run into a multitude of difficulties due to the types of dealings.

Chairman Frank: I don't mean distributing the amounts per person. I mean to say that the initiating underwriter should not receive more than a certain proportion of the spread in a particular issue.

Mr. Sweeney: I do not believe I would favor that. The tendency is, of course, that if the profit per bond is decreased, underwriters will keep more bonds for retail distribution, thereby securing the same profit and causing increased centralization.

A selling group to be successful requires that firm bonds must be offered in order that the effort necessary for successful selling may be gone through. Offerings made subject to subscription and allotments simply won't work.

Customers want to know if they are going to get the bonds when you offer them. On a fast deal, no bonds are available for the small dealer and this will cause him to give up the whole thing.

Firm bonds on fast as well as slow issues are important.

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I believe, in closing, that the small dealer business will be greatly hurt by competitive bidding, and I hope that the rule will not be adopted.

Chairman Frank: Thank you, sir.

Mr. Stewart: Mr. Herman Joseph.

STATEMENT OF HERMAN B. JOSEPH

Representing Joseph Co., Inc., Cleveland, Ohio

Mr. Joseph: My name is Herman Joseph. I am the head of Joseph and Company in Cleveland. I am a very much smaller dealer than Lowry Sweney. If other facts are necessary, I read both the utility division report and the I.B.A. report without getting the "flu" or anything else.

My business is strictly that of dealing with private investors. Less than ten percent of our sales are made to banks or institutions. As a house policy we do no underwriting. We participate in selling groups of securities of distribution. We reserve to ourselves the right to decide which selling groups we shall be in and which we shall be out of.

We have consistently followed a policy of recommending to our clients only those issues which appeal to us, regardless of who the underwriting house may be. We think our function is to select from the securities on the market those which are suitable for our clients.

Now, I view the introduction of compulsory competitive

arl5 bidding with a good deal of alarm from my own situation because on the experience which we have so far with issues which are purchased in that manner, our position is materially worse than it is on negotiated dealings.

Our experience, of course, is confined now to equipment trust issues, municipals, and the limited number of utility issues which have been sold at competitive bidding.

As a philosophical point, there seems to be, and there definitely is, in my case, a difference in the underwriter-dealer relationship on a negotiated deal and one which is purchased by competitive bidding.

If I may summarize what happens to us, this is probably the simplest way to do it. We have no fault to find with the number of bonds we are allotted or with our position in underwriting groups of negotiated issues, but our experience to date on the other type of issues is as follows:

We have never yet been offered a participation in a equipment trust issue. We have never yet been offered bonds in a public utility issue which was purchased at competitive compulsory bidding. We are offered municipal bonds, and here I distinguish between the small local issues and confine my remarks only to those issues of national importance--Boston of Philadelphia, or New York bonds--we have never been offered municipals of that type unless either the issue was distinctly sticky and hard to sell, or the house which purchased the

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bonds purchased them at an excessive cover over the second bid, in which case we seemed to be automatically included in the offering. Or, third, in a very limited number of very big municipal issues, such as the recent New York issue where there was one bidder, and there our operations are hampered decidedly by the fact that the margin of profit offered us in relation to the underwriting profit is distinctly on the low side.

May I then summarize very briefly to say that up to date our experience with issues originated in that manner has been decidedly unsafe. It has really hurt our ability to deliver securities to our customers.

Mr. Stewart: Mr. James, of Dallas, Texas.

STATEMENT OF JUD S. JAMES  
PRESIDENT, JAMES STAYART & DAVIS, OF DALLAS, TEXAS.

Mr. James: Mr. Chairman and Gentlemen, Jud James, President of James Stayart & Davis of Dallas.

Our business is confined principally to the retail distribution of securities in north Texas. I am still interested primarily in the time element on your Staff's report and the following remarks in this connection. I am frankly of the opinion that deserves more time for study than has been given those of us who are so vitally concerned. I should like to pay tribute to the public Utilities Division, that if this subject of bidding was so worthy of nine

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months' study by its experts in the time it took to write then it should be worthy of a thorough digest by the thousands of persons over the country who will be so deeply affected and, I believe, injured.

As a matter of fact, this report has not even reached many of the dealers and other interested parties in my section of the country. This, I am sure, is also true of the other distant sections such as the Pacific Coast. I heard of this proposal only last Wednesday.

I received a copy of it only last Friday, and while I have read it, I certainly have not had the time to give it the study that it requires.

I should like to inquire what, if anything, necessitates a major operation of this kind upon our economic system in such a hurried fashion.

After all, we have a system that has been functioning successfully as long as there has been a United States.

dk6

Chairman Frank: May I interrupt you to recall to you the facts that I narrated?

Last year the Commission sent out broadcast a questionnaire on this subject. It received responses. It might have acted on the basis of that questionnaire and the responses. That was many, many months ago.

The representatives of the N.A.S.D. or the I.B.A. did not hide their light under a bushel. As I recall it, the response of the I.B.A. to that questionnaire was published in most of the principal newspapers of the country, in almost ex-tenso.

It took a page of several papers. There must have been some sedulous effort to get that done, because it all came out on the same day.

The Commission, as I say, having made that request last year -- early last year -- might have acted upon the basis of the responses then received, and, had it done so, no one could warrantedly have said that the Commission was acting precipitately.

However, the Commission's staff took the replies, digested them, considered the arguments made in them, and presented those arguments to us.

The Commission might have taken those arguments, issued a rule, and stated its reasons for the rule by adopting, in whole or in part, what the staff reported.

Instead, the Commission thought it wise, before it made up

dk7

its own mind, to send out, as it did on December 18, the new report of the Staff.

The Commission then extended the time for receiving comments, and it has been over a month since that report was sent out, and fixed this time for a hearing.

Now, we endeavored, in every way, to give an opportunity to be heard, but I repeat again that the subject was broached by us and requests made by us, and they were broadcast.

Do you happen to be a member of the N.A.S.D.?

Mr. James: Yes, sir.

Chairman Frank: I am sure you must have received notice at that time of the N.A.S.D. reply to our request of last spring.

That couldn't have been concealed from you. I think you would have had to be pretty deaf not to have heard what the I.B.A. said about the matter at that time.

Since that time the officers of both associations, and particularly the I.B.A., have been going around the country making speeches on the subject.

At the last convention, the I. B. A. discussed the subject.

That was before our report went out.

As I say, the Commission could, on the basis of the replies it received last year, have proceeded to make up its mind as to whether or not there should have been a rule.



dk8

Now, to suggest that -- we haven't yet decided what we are going to do -- but to suggest that our decision has come or the contemplation that we are about to make a decision has been a secret and that we haven't been advised and haven't requested advice many, many months ago, is contrary to the record facts.

Mr. James: I didn't mean to leave the impression, Mr. Frank, that I didn't know what was going on, but I do think that, with a document as long as the report I received Wednesday -- Friday -- that some time should be given to a thorough discussion of the matter.

I am way off down in the country.

Chairman Frank: Now, we have received comments on the report from all over the country, many of them from Texas. Interestingly enough, all of them from Texas came in all on the same day.

Mr. James: Well, I had something to do with that.

Chairman Frank: Interestingly enough, all of those from St. Louis came on the same day -- on a different day; they were staggered by geographical areas.

The N. A. S. D. Bulletin for December gave a full digest of the report.

I think most of the dealers -- doubtless you do -- read either the Wall Street Journal or the New York Times or the New York Herald-Tribune.

dk9

There was full discussion of the report in those journals.

As I say, I don't think there has been anything in the way of concealment here.

Mr. James: I didn't mean to leave that impression. I am sorry if I did, but I still think we should have a little more time.

Do you mind if I finish this?

Mr. Stewart: May I interrupt, Mr. Chairman? I think it is a fact that our conference today is dealing with the proposal contained in this report, this specific proposal.

Chairman Frank: Yes, or any other proposal.

Mr. Stewart: I think that Mr. James was addressing himself to the fact that he did not receive this proposal.

Mr. James: It won't take me but a minute and I will be through.

The English, from whom we take so much of our law and procedures, have found the same system successful.

Now we are told by the Public Utilities Division that our past procedure was all wrong and that compulsory bids are so necessary that we must reverse a hundred years of practice with virtually no opportunity for widespread consideration and study.

Chairman Frank: You understand, of course, that this has nothing to do whatsoever except with subsidiaries of public

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utility companies, which are not industrials but are regulated enterprises -- you understand that?

Mr. James: Yes, sir.

Chairman Frank: And you understand that several states and other commissions have required compulsory bidding on such securities?

Mr. James: Yes, sir.

Chairman Frank: And that in New England two states have had that for many, many years, so it can't be said that this is a startling innovation.

Mr. Stewart: I think the fact is that three states out of 48 have such rules, rather than many of the states.

Chairman Frank: I didn't say "many of the states". I said there are several states that had it.

The Federal Power Commission has such a rule, I believe. The District of Columbia Commission has had for several years such a rule.

Mr. Stewart: While we believe, Mr. Chairman, that the Commission, of course, is correct in saying that its rule specifically relates only to the securities of registered public utility holding companies and their subsidiaries, we fear very greatly that the effect of the rule would extend far beyond that.

Chairman Frank: I have difficulty in understanding that.

Mr. Stewart: We doubt whether you can keep it quite in

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that bracket.

Chairman Frank: I don't understand the suggestion. Do you mean this: that if this Commission, acting in that restricted sphere of a particular type of company, which is known as a public service company, and subject to regulation in virtually all states of the Union, that if the Commission acts in that sphere, that Congress may be influenced by that fact and extend somebody's powers to regulate such activities of other corporations?

We do all sorts of things under the public utilities Act and Congress empowered us to do all sorts of things under the Public Utility Holding Company Act that we couldn't possibly do with respect to any other corporation, and which no one has ever suggested should be done with respect to it.

The very preamble of the Public Utility Holding Company Act shows that Congress recognized that it was dealing with a particular type of enterprise, which had its own peculiar problems, and the suggestion that somebody, by example, may get something done under this Act and apply it elsewhere, I don't see how that is quite germane to your discussion.

Mr. Stewart: Because of our great respect for the authority and prestige of this Commission, because we know what it does can not fail to have a great effect on what is done elsewhere.

Chairman Frank: Let me say, so far as I am concerned --

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I speak for no one else but myself -- I have no intention of suggesting the application of competitive bidding to any one except the securities that are under our jurisdiction, under the Public Utility Holding Company Act.

There is no suggestion -- of course, we haven't the power, nor are we urging that it be applied elsewhere, even if we adopt this rule.

Mr. Stewart: I am sure that is right, but it is a fact, too, that one of the Commissioners sits with a great many other state commissioners, the National Association of Railroad Utility Commissioners.

What this Commission does and what the members of this Commission do, will undoubtedly affect the judgment of those men and the administration of the laws with which they are charged.

We are also aware of the fact that immediately following the publication of the Commission's statement, that it was about to give consideration to this rule, we saw in the press the letter addressed to the Chairman of the Interstate Commerce Commission following it up immediately, so we can't believe that what you do here is confined merely to this one problem.

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Chairman Frank: Well, the Interstate Commerce Commission was long a pioneer so far as we are concerned. They had a competitive bidding rule on equipment trust certificates before this Commission was born. I don't think that we have much to teach them on the subject.

Mr. Stewart: You might teach them to recover from the mistakes they made in putting that rule into effect.

Mr. James: Mr. Frank, all I would like to ask is that you give us time to read this report carefully and make a study of it, and to read the replies of the I. B. A. and the N. A. S. D., - with which I will sit down.

Chairman Frank: Thank you very much.

Mr. Stewart: Mr. Cunningham.

STATEMENT OF S. K. CUNNINGHAM,

President of S. K. Cunningham & Company, Pittsburgh, Pa.

Mr. Cunningham: Mr. Chairman, and gentlemen:

Under date of January 17, 1941, I submitted in a letter addressed to Mr. Frank as chairman of this Commission a summary of the views of myself and my partner on this subject of competitive bidding. I shall confine myself to what I said there as a basis of elaboration, and on the one particular point in regard to the effect of the proposed rule on the small dealer.

In one paragraph of that letter, I stated that the report of the Commission's staff apparently implies that competitive

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bidding would work to the advantage of the small dealer outside of New York City. I am very much pleased to learn from Mr. Frank's remarks today that I have properly interpreted the viewpoint of the Commission. I have felt all along that the attitude of the Commission toward the small dealer is perfectly fair. On the other hand, as a local dealer I do not ask the Commission to pull our chestnuts out of the fire or defend our case for us, although we appreciate the fair attitude on their part.

The report of the staff, which I have not read completely, I confess, and which I think I would not have read if we had had it before us for six months instead of one month - so I present no alibi there - I read a summary of it, and as suggested, we have all had this question of competitive bidding in our minds for years, and I think we have plenty of background on which to base an opinion.

The small dealer, the local dealer, is the chief contact between the issuing house and the investing public. Whether we recognize it or not, the average buyer wants opinion or suggestions. It is human nature that people will not make up their minds, by and large, until they get some person to confirm the opinion which they already have, even. That is why a lot of people go to church and go to all sorts of meetings, they enjoy it when the preacher or speaker confirms what they already believed when they went there.

Chairman Frank: That is why Mr. Stewart is enjoying what you are saying. (Laughter.)

Mr. Cunningham: If the speaker tells them something they do not already believe, they don't like it. So they want that opinion. They come in with their mind entirely made up, but they still want you to tell them that that is the thing to do.

But aside from that, they need more information, and I don't know how in the world they are going to get it since the commercial banks are not in the business of selling securities any more except through the local dealer. And they are not getting it. I beg the privilege of putting in a parenthesis, Mr. Frank, they are not getting it through the 50 or 100-page prospectuses which are used these days. I have no quarrel with the prospectus and the disclosure of full information; it is good and should be continued; but, gentlemen, it is not practical to send out those prospectuses to a hundred prospects, and so they do not get the information, and if they did get a prospectus, they would not read it. We should be allowed to send out a summarized form - but that is off this subject, and I apologize and I end that parenthesis.

Chairman Frank: It is a very handy set of punctuation marks.

Mr. Cunningham: Now, in regard to this question of concentration of power which your staff's report referred to in connection with the small dealers, it may be that there is



too much concentration of power, but that is not the thing we are discussing now, and anyhow, when it comes to the large public utility issue, how can it be underwritten and sold either by competitive bidding or otherwise except by organizations that are strong enough to take that commitment? And I, as a small dealer in Pittsburgh, have no quarrel, therefore, with those firms with sufficient strength - or those groups of firms that can do that. It is to my interest that there should be such firms and they give us a little share, a very small percentage; they do not give us enough break in the gross profit, Mr. Frank, but even on that I am willing to fight my own battles and argue that with them.

And there may be a time, if this rule is not put into effect, when we as a local dealer, and Mr. Sweney or Mr. Joseph or a lot of other firms, can handle a public utility issue that is within the range of our ability, and if competitive bidding is required in all cases, I feel that we would be forced between the two sides of a wedge, and our position would be much less secure and we would not have the incentive nor the profit opportunity to serve those investors which it is our function to serve.

I have no desire even to try to defend the position of the local dealer, as such, except as we fit into the economic structure and meet a necessary need. I believe we do that. I think we do not need any defense on that ground.

Mr. Joseph mentioned the experience of the local dealer with equipment trust issues sold by competitive bidding, and municipal issues, and so forth. Our experience confirms largely what he said on that subject. We have had large experience in municipal issues which we participate in and in the purchase of them in competitive bidding, and which we distribute, but I can not see that we get any better break there in the large general market of municipal issues due to competitive bidding, and our experience is that we get a better break and we are better able to serve our investors where the sale is negotiated.

Mr. Chairman, this covers my comments with respect to the subject which you raised as the first on the program. My biggest objection to competitive bidding does not come under this heading, and reserving the right of being given an opportunity to present it when it properly comes in, I shall close.

Mr. Daley (Of Otis & Company): May I ask Mr. Cunningham a question, Mr. Chairman?

Chairman Frank: Yes, go right ahead.

Mr. Daley: Is it not a fact, Mr. Cunningham, that on the note issues of utility companies which are sold by private negotiation in conjunction with bond issues, that the small dealer never gets any chance, either, at the note issues which are of the same term as the equipment trust issues?

Mr. Cunningham: I would not say that he never does. I

agree that it frequently happens that we do not get a chance at the note issues, and maybe we don't want it.

Mr. Daley: Isn't it also the universal practice that the top underwriting group take the short-term notes in those issues?

Mr. Cunningham: I think it is frequent, at least.

Chairman Frank: It occurs to me that we can try this suggestion: Without cutting anybody off, and nobody will be cut off, that we might turn profitably to another topic which will do more to center attention on specific subjects, and for that reason I suggest that we try going on to the second subject suggested by Mr. Stewart, a consideration of the probable effect of competitive bidding from the standpoint of the investing public with particular reference to the problem of over-pricing.

It seems to me that there, Mr. Stewart, the larger originating underwriters might have more to say, and it might be well to call on them in the first place with respect to that subject.

Mr. Stewart: Yes. May we have your indulgence for just one moment; Mr. Connely has a very short statement that he would like to make.

Mr. Connely: I want to correct one remark about our representing the large dealers. There has been a fallacy that has existed. We will admit that the N.A.S.D. is about four

times as large as the I.B.A., but the I.B.A. is financially supported to a very large extent by the small dealers. The biggest dealer-underwriter in the business pays the I.B.A. the sum of \$200 a year in dues. That same dealer-underwriter in the N.A.S.D. pays \$3,000 a year in dues, and the financial backing of the N.A.S.D. is preponderantly done by the large underwriters, and the preponderant financing of the I.B.A. is done by the in-between and small dealers.

Mr. Stewart: Mr. Chairman, if you please, there are some gentlemen here from non-underwriting houses that really represent the investors, and I believe that it would be in the interest of some of them who would like to get away, if we heard from them.

Chairman Frank: Yes. I merely suggested that we might make progress if we got some of the larger houses addressing themselves to this question, and then have the others do likewise.

#### STATEMENT OF CLOUD WAMPLER

President of Stern, Wampler & Co., Inc., Chicago, Illinois.

Mr. Wampler: My name is Cloud Wampler; I am President of Stern, Wampler & Company of Chicago.

As a matter of background, let me point out that our organization, which operates almost entirely in the Middle West, is primarily engaged in the sale of securities to individuals. In other words, our business is largely with

private investors rather than institutions. Furthermore, we originate few issues of any kind, and practically no public utility securities. Accordingly, my chief interest in the proposal to compel utility companies to seek bids for their issues of securities is largely this: Will the new system help or harm the private investor?

Whenever an investment banker is faced with the problem of advising an individual investor regarding a security purchase, the following three fundamentals are considered:

1. Is the security sound?
2. Is it properly priced?
3. Is it an appropriate addition to present holdings?

It is my best judgment that "competitive bidding" will tend to damage the interests of the private investor with respect to quality and price, and will impede the making of proper additions to present holdings.

As to quality, it should be borne in mind that bidding is not merely a matter of price. Organization A may bid 100 for an issue with numerous restrictions designed to safeguard the investor, which restrictions are naturally somewhat of a burden to the issuer. Organization B may bid 100 - or even slightly higher - for the issue in question and offer far less onerous restrictions.

Chairman Frank: You understand that there is nothing in the proposed rule that says that the highest prices, regardless

of other circumstances, must govern?

Mr. Wampler: I understand that perfectly. On the other hand, there will certainly exist a great temptation on the part of the issuer to accept a combination of a high price and less onerous terms.

Chairman Frank: You also understand that here you are dealing with a security which is subject to our regulation and supervision?

Mr. Wampler: I do, indeed.

Chairman Frank: And I do not think that we have been notorious for our laxity in that respect.

Mr. Wampler: I certainly do not mean to imply that. On the other hand, we have had in a financial experience, over a long period of years, groups of people develop as specialists in certain fields, and I would feel safer in my work with the individual investors to have an indenture, the set-up of which was passed upon by people highly skilled in the business in whom I had confidence, supplemented by your own checks and balances.

To continue: If the offer from B is accepted - and presumably it would be - the issue offered to the public is not as high in quality as required by A, and the investor is therefore not as well protected.

It is undoubtedly true that intensive competition among investment bankers has in the past enabled many borrowers "to

write their own ticket" with respect to restrictive safeguards.

Commissioner Healy: If that is true, Mr. Wampler, it would seem that the regulatory body must have been pretty sound asleep.

Mr. Wampler: Well, Judge Healy, that sentence was injected into my remarks as a very broad statement, and I do not recall personally any public utility issues where that statement could probably be made, but I certainly can recall examples of industrial issues and foreign government issues where the statement holds.

Commissioner Healy: I would not doubt it at all in that field, but let us remember --

Mr. Wampler: (Interposing) I happen to share Mr. Stewart's views regarding the possible influence of competitive bidding in one field upon possible competitive bidding in other fields.

Commissioner Healy: You have put your finger on what is a very important difference between the two classes of securities. In the general commercial and industrial field, there is practically no supervision or regulation over the terms of the issue. It has to be traded out between the issuer and the underwriter. Here, on the contrary, are State and Federal regulatory bodies which have all kinds of authority over the terms and the conditions of these issues, a feature that is completely lacking in the other field.

Now, what do you think would happen if an issuer and an

underwriter came in here with an issue where the terms of the indenture were very poor from the investor's point of view? Do you think that it would get by?

Mr. Wampler: No, I certainly do not; not for one minute.

Chairman Frank: You see, our experience up to date has been very largely in the negotiated issues of utility securities, and we have had to attach conditions and require better standards in many instances. Your remarks might be interesting in some other field, but let us confine our remarks to this particular rule and our powers. We have not anything to do with competitive bidding in other fields - we are assuming that we have it for public utility securities - but we have not any power outside of that.

Mr. Wampler: In making what I thought were broad-minded admissions about the vulnerability of my remarks, I do not want to find myself in the position of admitting that in my judgment the restrictions incident to the public utility bonds purchased under compulsory competitive bidding are bound to be just as good as under negotiated bidding.

Chairman Frank: Our experience has been, I may say, that we have not frequently had to see that a negotiated deal was relaxed because the conditions were too harsh.

Mr. Stewart: If I may say so, Mr. Chairman, we had hoped that the matter of indenture conditions might be discussed under another heading.



Chairman Frank: Whether they be indenture provisions or otherwise, we do not find that we have to step in and insist on relaxed terms on exceptionally harsh terms between the banker and the issuer.

Mr. Daley: Even when the so-called best bankers bring an indenture down here, it has been the practice quite frequently for the large investor to insist that there be better restrictions in the indenture than the so-called best bankers had already incorporated.

Mr. Stewart: I don't know, Mr. Chairman, whether this pamphlet represents the view of Otis & Co., but I see in it the statement that competitive bidding will relieve the banker of spending a great deal of time and work in the preparation of documents, which of course goes directly against the professional aspect involved in this discussion.

Mr. Daley: I don't think it does, and we will be glad to go into that subject very carefully whenever the Chairman is ready to hear it.

Commissioner Healy: Of course, Mr. Wampler, another element which might be given some weight in the public utility fields, and most other fields, is that rates and prices are regulated in the utility field and they are not in the other - that is, not to any extent.

Mr. Wampler: I firmly believe that damage to the individual interest of the buyer of bonds and stocks is more

apt to involve the matter of price rather than quality. Data has been compiled which indicates that the price behavior of public utility bonds purchased by negotiation is better than that of issues sold under competitive bidding. I believe data has been developed to prove the contrary. Based on the compilations that I personally have studied, it would seem that during a period of a few weeks immediately subsequent to the public offering dates, that the negotiated issues advanced modestly in price, while the bulk of the competitively bid in issues behaved less well.

Chairman Frank: Mr. Weiner wanted to ask a question.

Mr. Weiner: I wanted to ask with respect to those issues where the indenture has turned out so poor and your mentioning some values of bonds and industrials, - who it was, if you recall, who drew those debentures?

Mr. Wampler: I certainly can not give you that information here, but I will be glad to give it to you.

Mr. Weiner: We would be glad to have that information.

Mr. Wampler: It may be said that there have been so few issues placed under competitive bidding that such statistics mean little. If that is the point of view, I have not any quarrel, but it seems to me that there are certain things inherent in compulsory competitive bidding that we have got to be a little fearful of. I am inclined to think that the very spirit of compulsory competitive bidding as opposed

to that of negotiation tends to make cool judgment a little bit more difficult.

I believe that competitive bidding provides the means for an organization to buy its way into a certain field, and unfortunately the purchase price is usually the public's money.

I am sure that in competitive bidding, the element of pride becomes an important factor, and the urge to head a piece of business may easily cause too high a price to be paid for the issue; and no matter how high a price is paid for a given issue, a very large part of it will be sold at retail, and the slower the deal, the more of it will be sold to private investors as opposed to professional buyers. So it will usually be the individual buyer who is hurt.

Our organization is firmly convinced that those four factors are part and parcel of competitive bidding, and it is because of them that we have, over the years, preferred not to handle corporate issues that are bid for. Of course, that field is not very large; it includes a comparatively small number of public utility issues and equipment trust issues. We base that reluctance to handle bid-for securities on an experience of having sold some of them to our clients, and usually there is a price recession, and the customer has lost money, or at least he thinks he has, and that is the point that leads me to an expression of opinion that competitive

bidding will make it more difficult to induce private investors to make appropriate additions to their holdings.

This point that I am going to try to make now is something that has occurred from time to time in our own shop. We believe strongly that private investors should buy high-grade bonds today. Getting them to buy high-grade bonds today is --

Commissioner Healy: (Interposing) Let me interrupt you right there. You say you think private investors should buy high-grade bonds today?

Mr. Wampler: Public utility bonds.

Commissioner Healy: Are you thinking of people of large means, or people of average means?

Mr. Wampler: I am thinking of both, to hold.

Commissioner Healy: Now, as applied to people of average means, do you think that a 3-1/4 percent coupon at 107-1/2 is a good bond for a private investor of average means?

Mr. Wampler: Probably not, but I could think of lots of good public utility bonds that would come within the scope of today's discussion that I believe are very good purchases for a private investor. And let me emphasize --

Commissioner Healy: (Interposing) I assume, then, that you will agree that a great many of them are going out now at these prices that are really institutional bonds, and do not belong in the portfolio of a person of small means?

Mr. Wampler: Certainly.

Commissioner Healy: All right.

Mr. Wampler: But good bonds certainly have a place in the average individual investor's account. But the sale of these bonds - let us take just a rough example of a 3-1/4 percent bond that might become available at par or 101, the resistance of the individual investor to that offering is great, and it takes considerable salesmanship to convince him that he should maintain the degree of quality that the purchase of that bond will enable him to maintain.

That selling process is not easy, and it becomes particularly difficult if the client has recently bought part of a high-grade issue that promptly sold off in price, and anything that tends toward over-pricing of issues and the subsequent decline, particularly if the decline takes place promptly, makes it very hard to get the average individual investor to buy these securities, and unfortunately he turns almost automatically to high-rate and less sound issues.

Another point in this connection is that private investors are loath to buy any issue purchased by a bidding group at a price very much in excess of that offered by the next highest bidder. And it is not at all unusual under "competitive bidding" to see a "cover" of \$10 per \$1000 bond or so. He believes that the person that covered the second bidder by \$10 a thousand has just made a gross mistake in the evaluation of the

price of the bond.

Chairman Frank: The consequence of that would be, I would think, that if you had a general competitive bidding rule applied to utility securities, and a group bought and, to use your terminology, paid an excessive price, they would not do it again.

Mr. Wampler: They certainly would eventually come to the end.

Chairman Frank: But I mean that one experience - the first experience of the group that over-bid in the sale of its securities, would find a difficulty in selling the securities, and according to your thesis that would teach them not to do it the second time, and the consequence is that your fear of over-pricing would be offset by the knowledge on the part of the persons buying at an excessive price that they would have difficulty in selling.

Mr. Wampler: I hesitate to make this remark, because I am not absolutely sure that I am right, but I seem to recall in the case of some competitive bidding not very many years ago where the same man made two very large covers within just a few days, or at the outset two or three weeks of each other. There is a tendency on the part of houses during a certain stage of financial history, so to speak, to try to buy their way into pieces of business, and if public utility companies advertise for bids, and so forth, I think you will find a

good many people trying to get into that business by paying a very high price for securities.

Chairman Frank: But according to your statement, the intelligent investor observing that fact won't buy, so that the investor won't be hurt, and it will be the buying house that is.

Mr. Wampler: I don't think so.

Chairman Frank: That seems to be the logic of your position.

Mr. Wampler: I say that when there was a great big covering, but it does not necessarily follow that there will always be a great big cover.

Mr. Stewart: I think we can demonstrate specific examples of that as we go along. If there is anything wrong with the logic, it is not with the facts.

Mr. Wampler: Our organization is convinced that if competitive bidding becomes compulsory, that another disadvantage for the private investor is that many of the good medium-grade public utility bond issues will become absolutely unavailable to private investors, especially to those located in cities other than the leading financial centers.

Mr. Daley: Mr. Chairman, one comment on Mr. Wampler's statement. I presume that we are discouraging the private investor in some respects by the fact that on privately negotiated issues, such as Jones & Laughlin, Crucible Steel,

and others, also sold immediately off in price. I don't think that selling off is confined, by any means, to competitively bid issues. I have one further remark, and that is, I think that on the subject of over-pricing and its effect on the investor, that I would like to suggest that if they want to get a discussion on the other side of that, that the Kuhn-Loeb memorandum of 1922 be read, in which it was pretty well brought out that the railroads would not get enough money for their issues if it was competitively bid.

Mr. Stewart: We submit that the evils of excessive competition attend issues which are apparently privately negotiated, as well as those sold under the rule requiring competitive bidding.

Chairman Frank: Will you repeat that statement, Mr. Stewart? I did not get it.

Mr. Stewart: We submit that the evils of excessive competition attend issues, apparently, which are privately negotiated, as well as those sold under a rule requiring competitive bidding.

Chairman Frank: I would like to hear, now, from those people who are initiating underwritings. I would like to hear from one of the large houses, if you don't mind, on this topic. I see several representatives here of the large underwriting houses. If they care to be heard, I wonder if they would care to be heard now.



Mr. Stewart: I have no knowledge of that.

Chairman Frank: Are there any that care to be heard on this subject? Mr. Stanley, do you care to be heard?

Mr. Harold Stanley (Of Morgan Stanley & Co.): My name is Harold Stanley, of Morgan Stanley & Co. I understand, Mr. Chairman, that you would like me to speak about prices now? I am perfectly ready to speak now or later, but if you would like me to speak about pricing now, I would be very glad to and go into other things later.

Chairman Frank: What would you care to do; what would be your preference?

Mr. Stanley: I am not pressed at all. If these other people want to get away, I can speak later.

Chairman Frank: I think it would be desirable if you make a statement on this subject, and then we will hear from the others.

Mr. Stanley: I have here a memorandum, which I would like to submit later during the hearings, in which we take a position of disagreeing very completely with the report of your staff. I won't go into other matters now except as to pricing. We have a list here or a table which summarizes our actual experience on 74 issues which have been managed or co-managed by our company to December 31, 1940. These issues total \$2,684,099,000 face amount. The offering price was an average of par-52. The bid price on the first day was par-82.

The bid price the second week was par-89. The bid price the third week was par-87. The bid price the fourth week was par-86. So that, at the end of the fourth week, there was an increase in the price of about .34 percent. I think that indicates the fairness of the prices arrived at through negotiation as measured in the subsequent market for a short period afterwards.

Of course, the market may have gone up slightly during that time, or down. This is the average figures on five years of work.

Commissioner Healy: Did the syndicate carry on any stabilizing operations during that period?

Mr. Stanley: Yes.

Commissioner Healy: Then I do not see that those prices mean anything.

Mr. Stanley: By the fourth week, the stabilizing operations had ceased.

Commissioner Healy: If you will give us the prices after the stabilizing influence on the market had stopped, and supply and demand is really working freely, then I would be interested.

Mr. Stanley: I am sorry that I have not those, but I think that these are indicative. You will notice that these are, on the average, slightly above the offered prices. Is that sufficient?

Chairman Frank: Is that all you care to say?

Mr. Stanley: I will be glad to comment on anything you like.

Chairman Frank: Mr. Eaton, do you care to be heard on this subject?

Mr. Eaton: No.

Mr. Stewart: Mr. Chairman, if I may say it, there are several gentlemen here representing investors who would like to get away today, and they would appreciate it very greatly if they could be heard.

Chairman Frank: Yes, indeed.

#### STATEMENT OF FREDERIC P. FISKE

Vice President and Director, Montclair Trust Company

Montclair, New Jersey

Mr. Fiske: To save the Commission's time and those of the other people here, I have written out a very brief statement.

I wish to say at the outset that I express no views whatever on the collateral arguments raised by both the proponents and the opponents of competitive bidding. They are of no direct concern to me at the present time. As an executive officer and director of a moderate-sized trust company, and as a member of the Finance Committee of a small insurance company, I am interested in the subject only as it may affect my ability to buy for our bank and for our customers and for the insurance company, high-grade securities at fair prices.

In my opinion, competitive bidding produces a result that is contrary to our interests and contrary to the interests of our customers, and to that extent, and that extent alone, it becomes a concern of mine. It is my belief that one major duty of the Commission under the law is to protect investors.

I represent a group of small investors, and I feel that competitive bidding assists in raising security prices to the detriment of this group; hence, I hope that the Commission will give adequate consideration to this phase of the question before compelling utilities to sell securities by competitive bidding.

For a great many years I was in the securities business, but for the past 7 years I have been interested solely as a buyer for small institutions, and hence my interest is with them and their problems.

In the insurance company, we have a portfolio of about \$7,000,000, and have about \$600,000 this year to invest.

In the bank, we have a combined portfolio of about \$7,500,000, and some \$24,000,000 of resources in our Trust Department.

As you know, investment officers everywhere are having a frantic time finding suitable investments, and the prevailing surplus of funds and the scarcity of bonds has created a market the like of which I have never witnessed. At times, almost any decent issue will go at any kind of a price. Such

a situation created a steadily rising trend of prices in which each successive issue could be pushed up a little as compared with comparable issues already outstanding, and this rising momentum has been checked only occasionally when some of the large insurance companies temporarily stepped out of the market. The scramble on the part of investors has had its reaction on the dealers, who in turn have had to scramble for their merchandise.

This has resulted in gross over-pricing of several notable issues during the past two years whenever a competitive bidding situation has developed.

In the summer of 1939, there was the Southern Bell Telephone bonds, the Terminal Association of St. Louis bonds, and earlier in the year there were the Chesapeake & Ohio Railway bonds, <sup>although</sup> A low public bidding was not called for in each case. As I understand the situation, an equivalent situation was created which resulted in the bonds being brought out above the then existing market, and the prices broke when the syndicates dissolved.

Commissioner Healy: I would like to know the basis of your statement, so far as that Insull issue is concerned - that Central & Southwestern issue.

Mr. Fiske: I made no mention of a Central & Southwestern issue. I said the Southern Bell Telephone.

Commissioner Healy: I beg your pardon.

Mr. Fiske: The three issues I mentioned, Judge, are the Southern Bell Telephone, the Terminal Association of St. Louis, and the Chesapeake & Ohio Railway.

Recently we had a direct example of over-pricing as the result of competitive bidding in the Boston Edison bonds. The First Boston Corporation obviously bid to get the bonds, probably feeling that in a strong market the rising trend would catch up with the advanced price and move the bonds along, as had happened with so many over-priced issues in the past few years.

For a variety of reasons, this failed to happen, and what would have been a most successful issue at a reasonable price was not so successful when the bonds were priced too high.

From my past experience, I imagine that the bidders, who I believe numbered three, first figured out in their own minds a fair market price, and then added to it what they thought necessary to beat the competition, and as the market had been favorable up to that time, they figured the maximum price which they could possibly pay without being too badly stuck if something went wrong. This has been the type of thinking forced into the securities business ever since I can remember when a competitive situation developed. I remember it well from my own past years in the securities business.

When the Edison bonds were offered, we, in our bank, were in a dilemma. We had about \$150,000 of the old bonds in trust

funds. Comparable issues were scarce, and none were available below their call prices. We felt that the bonds were too high, but we had idle cash to be invested. Should we take a chance and wait to see if the market would break? We called our Investment Committee together and discussed the matter at length. As you know, you can not leave trust funds uninvested, and if the market picked up and moved the bonds up, as had happened many times in the past few years, and if we had not bought, we could never have justified our failure to make those purchases.

We bought some bonds, and you all know what happened. We were forced into paying <sup>+00</sup> much for the bonds because bidding had been competitive. If, on the other hand, the company had used an established banking contact and someone had been on hand to urge on the company a fair market price, I feel that the bonds would have come out considerably lower. The market would not have broken and we and many other small investors, who were so unfortunate as to buy as soon as the offering was made, would have saved a considerable sum of money.

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Commissioner Healy: May I ask you there if you have ever paid too high a price for bonds that were not sold through competitive bidding?

Mr. Fiske: Undoubtedly. But in the market such as we have had, Judge, in the past few years, it has lent itself to competitive bidding because a person could pay above the existing market, and unless something happened, as happened in the past few weeks, they could sit back and there was a fair assurance that the market would move up and take the bonds, but the people who came in and bought the day the issue was first offered, almost inevitably got stuck and they certainly got stuck if the market in the meantime turned.

Mr. Weiner: I wonder if the First of Boston which has just been mentioned and has had its practice described by others -- I wonder if they are here and they would care to say whether that was a correct statement as to how they arrived at their bid?

Chairman Frank: We can hear from them later. They have a representative here.

Mr. Fiske: I am only interested in getting these bonds cheap; I don't care about all the rest of it.

(Laughter.)

One other point. I believe that a careful conscientious house of issue provides an element of real protection to investors when it has an opportunity to help work out an issue,



and I do not see how it is possible anyhow to work out an issue and impress its influence on that issue in the haste and excitement of competitive bidding. I feel that since some of my views are already in the Commission's possession -- I have had some correspondence with Commissioner Pike -- that more extensive comments by me are repetitious and are unnecessary, but I do respectfully urge the Commission to consider the point of view which I represent and I sincerely hope that it will refrain from ordering competitive bidding.

Commissioner Healy: Have you examined any of the terms of the issues or indentures of the companies which were sold competitively in New Hampshire and Massachusetts to see how those indenture provisions compare with the provisions of other issuers not sold competitively?

Mr. Fiske: No sir, we do not have time. That is another thing that I did not want to bring in here. When an issue comes along these days, we won't have time to examine anything. Someone offers it and you are not able to get a prospectus and you don't know anything about it and you have to make up your judgment of it too hastily.

Chairman Frank: You are then suggesting that the old 20-day rule was desirable?

Mr. Fiske: No sir, because that did not help us either. We were not able to get the prospectus.

Chairman Frank: You think you should have time to get

prospectuses?

Mr. Fiske: We should get something.

Commissioner Healy: You have a prospectus at the time that you get the bonds.

Mr. Fiske: Yes, but unfortunately by the time they deliver that prospectus, we have bought them.

Commissioner Healy: In other words, your point is that the time a fellow needs a prospectus is when he makes up his mind and not when he gets the security?

Chairman Frank: We will be interested to have you advise us with respect to that subject on proposed amendments to the Securities Act.

Mr. Fiske: I have got a bank to run.

Chairman Frank: We are interested in protecting your bank.

Mr. Fiske: I think you are.

Chairman Frank: We would like to get your views in extenso on that subject -- some other time.

STATEMENT OF WALTER E. SACHS,

of Goldman, Sachs & Company.

Mr. Sachs: I do not want to take up the time of the Commission for one moment because I have not prepared any statement, but I want to say a word on this question of overpricing.

I take it for granted that the ideal is that securities that are issued should be priced as accurately and fairly as possible both from the point of view of the issuer and from the point of

view of the investor. It seems to me that what is lost sight of is that the real competition that we have at all times is what I call the competition of the market, and by that I mean under the present system where the house of issue is in consultation and is in negotiation with the issuer, the competition of the market is always present, and that a close study has to be made of comparable securities and the prices of comparable securities, and it frequently happens in issues between the issuer and the house of issue that has had a continuing relationship with the issuer, that the others may come in and even offer a somewhat higher price, and that then in the discussion of market conditions, and the discussion of market prices of other comparable securities, a fair price with a proper spread can be arrived at which results in the security being issued at a price which is as accurately and as near the price of the other extant securities as may be.

The haste, on the other hand, and the desire for business which might come and which has come frequently from competitive issues, is, in my opinion at least, not nearly as accurate an estimate of what the price should be as the closer study on the part of two fair men or two fair interests on both sides of the picture.

I think that we will find that while there have been mistakes made both ways at times, mistakes of judgment in negotiated issues, that on the whole this competition of the market, the competition of what securities of a similar type are selling for,

is the most accurate estimate that can be secured.

As I said, I do not want to take up the time of this meeting, but I think that that is a fact that might well be taken into consideration.

STATEMENT OF CYRUS S. EATON

(of Otis & Company).

Mr. Eaton: Mr. Chairman: May I say just a word in response to Mr. Fiske's comment on the Chesapeake & Ohio bonds and the Terminal of St. Louis bonds? I do not regard this question of overpricing as a very fundamental one in this discussion. There are other issues that are of vast importance as compared to that, and I would like to have the privilege perhaps of referring to some of them later on, but on the subject of overpricing and with respect to the two issues that were mentioned as illustrations, we were joint account with Halsey, Stuart & Company in the purchase of the \$30,000,000 of C. & O., and in the Terminal of St. Louis bonds. There was an honest difference of opinion as to the value of the C. & O. bonds. We offered them at 101½. There were people who thought that they were overpriced. There were people of a good deal of influence who thought they were overpriced and who expressed their opinions freely on that subject, with the result that there was hesitation on the part of the investors in buying that bond at 101½, but no one purchased a bond from the Syndicate at less than 101½, and some of the most discriminating buyers in the country finally paid 105 for the bonds to the Syndicate, showing

that our judgment on that occasion happened to be sound and in accord with the market.

With respect to the Terminal of St. Louis issue, those bonds were purchased just a few days before the war was declared, and all issues went off, whether privately negotiated or otherwise. There was a big fall in the market and temporarily there was inactivity in those bonds, but later on --

Chairman Frank: (Interrupting) It occurs to me that there was something around that time about selling Bethlehem Steel, and that was a privately negotiated deal, was it not?

Mr. Eaton: And Pure Oil.

Chairman Frank: Yes, and Pure Oil. We heard quite a little about that. I don't believe those were competitively bid for, were they?

Mr. Eaton: Those mistakes occur, and if this system of free enterprise that we are all so much interested in is to continue, it seems to me that one has the right to make a mistake of judgment. That is the whole basis of our competitive system. It seems to me that one of the most enlightening discussions of this subject is found in Kuhn Loeb's brief presented to the Interstate Commerce Commission about 15 years ago when they were considering this same subject.

Chairman Frank: Do you happen to have a copy of that brief?

Mr. Eaton: Yes, I have one and will be glad to supply it.

They took the ground that the proper issue involved in that

discussion was the highest possible terms and price to the issuer. That was what they were seeking to sustain. And they held this, they said that if prices are to be supported and if issues are to go out at a high price, we must have banking houses who are of great influence and great prestige behind them, otherwise you will not be able to secure a full price for the security when it is offered, and furthermore unless you have that kind of sponsorship, the market on the issue will not be sustained and supported in bad times.

Well, that had a lot of influence with the Interstate Commerce Commission at the time, and they said, "If this thing is thrown open to competition so that anyone can buy an issue, markets will not be supported and securities will be sold at too low a price."

Commissioner Healy: How many examples can you give us of houses supporting issues that they had underwritten and distributed, and then going into the market and supporting them in bad times?

Mr. Eaton: Of course that just does not happen, Mr. Commissioner.

Commissioner Healy: In other words, that is a very thin slice of baloney.

Mr. Eaton: Yes. It is an argument that is a seductive one at the time that it is offered, but the experience of the banking world has demonstrated that practically every position taken by Kuhn Loeb and backed at that time by J.P. Morgan & Company in

connection with railroad financing -- practically every argument on which they based their case has been completely demolished in the 16 or 17 years that have elapsed since that time.

But that argument was so potent at the time that the Interstate Commerce Commission applied competitive bidding only to equipment trust issues. They said, "We will try it there. We are impressed with the dangers of adopting it everywhere, but if it works with equipment trusts, we will consider it elsewhere." And you all know the history of equipment trusts, the liveliest market in corporate securities, and dealers everywhere interested in them, they are short term, small spread, one to ten years mainly, but is there any security in this country that has a livelier and more active market than those?

Mr. Fiske: Mr. Frank, may I say one thing on this question of equipment trust issues? That competitive bidding has driven those issues up to such prices that they are no longer fit investments for small institutions.

Mr. Stewart: If I may suggest, Mr. Chairman, I think that we must deal with today's problems rather than with the problems of 19 years ago or more. I am sure that whatever Kuhn Loeb said at that time was good and well considered thought. I happen not to be familiar with the brief, and I doubt if there is anyone here from Kuhn Loeb to speak for them, and I suggest that if we wish to consider what they said 19 years ago as applicable to the situation today, that they be invited to come down and talk about

it.

An interesting point arises, too, in connection with the Chesapeake & Ohio issue which I suppose is as well a utility issue you would have had to deal with, and that is that the price of 105 I think which was paid was about a year or more later than the day of the offering. I don't think that 105 was offered until you offered some \$7,000,000 of the bonds one year after this first purchase, is that right?

Mr. Eaton: That is substantially so.

Mr. Stewart: It is interesting to note that lapse of one year in that particular issue.

Commissioner Healy: Mr. Stewart, are you going to be prepared before these conferences are over to tell us what sort of rules you think that we ought to have to deal with cases where there is an affiliation between an issuer and the underwriter?

Mr. Stewart: We will do our best, Judge.

Commissioner Healy: I would be very much interested in that subject. Our present rule has been criticized both inside and outside of the Commission. Whatever we do about competitive bidding, I think the subject of how to treat affiliated underwriters is something that we have to consider anyhow.

Mr. Stanley: In reference to the C. & O. price, the whole market went up four or five points, including the other C. & O. issues which were outstanding. So far as you refer to Bethlehem and Pure Oil, although we were not in that business, that had a



30-day standby on a market change.

Mr. Eaton: I would like to give you some figures on those C. & O. bonds.

Chairman Frank: You may each file your statistics.

(Laughter.)

Mr. Jackson: Last spring the N.A.S.D. did submit suggestions and a rule which it deemed appropriate to deal with the situation.

Chairman Frank: Yes, Mr. Jackson, we had a conference on the subject at which you were unfortunately not present, and we found great difficulty with the proposed rule with the conferees, and they promised to come back to us with their suggestions because of the difficulty. And I understand that you did come back with some further suggestions which we should like to hear this afternoon.

I experienced the same trouble that Judge Healy does. We have been told that competitive bidding won't do. If that is correct and if our rule U12F2 won't do and no other rule will do, then we are confronted with a real dilemma when we are confronted with the question of an issue being sold to someone as to whom there may be some reason to believe that he may be an affiliate.

Mr. Jackson: I simply want to say that we had made an effort in that direction.

Chairman Frank: We will adjourn now and reconvene at 2.30.

(Whereupon at 1.05 p.m., a recess was taken until 2.30 o'clock of the same day.)

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## AFTERNOON SESSION

(Whereupon, the conference was resumed at 2:30 p.m.)

Chairman Frank: Are you ready to proceed, gentlemen?

Mr. Stewart: Mr. Boyden, of Chicago, is here, Mr.

Chairman. He is going to speak, I think.

## STATEMENT OF WILLARD N. BOYDEN

Vice-President, Continental Insurance Co., Chicago.

Mr. Boyden: Mr. Chairman, Gentlemen of the Commission--

Chairman Frank: Will you give your name?

Mr. Boyden: My name is Willard N. Boyden and I am Vice President and a Director of the Continental Casualty Co. and Continental Assurance Co. of Chicago. The Casualty Co. is one of the larger stock casualty companies with assets of 40 million dollars. The Assurance Company is a smaller life insurance company with assets of 37 million dollars and 275 million dollars of insurance in force.

It appears to us that compulsory competitive bidding on utility issues would be harmful to the interests of the small and medium sized investing institutions as well as to individual investors. Our conclusion is based on three principal counts.

In the first place competitive bidding frequently results in excessively high offering prices to the public. In their eagerness to get business some investment bankers apparently are willing to stretch their bids to the last 1/8 of 1%. Their theory seems to be that if they can succeed in

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selling the whole issue at the offering price they will make a profit. If, on the other hand, they can distribute a major part of the bonds at list, they then, if necessary, can close the account, sell out the balance at a loss and still break even. In either case their sales organizations will have been busy and the overhead problem will have been helped. Occasionally, the winning bid turns out to be so high that the distributing effort is a serious failure and the banker sustains a loss.

All too frequently under competitive bidding, regardless of the type of security, the investor who buys at the original offering price does not buy at a fair price and soon finds himself with a paper loss.

In general, when the investor is contemplating the purchase of bonds of a new issue awarded under competitive bidding it would seem wise to be a little more careful than usual to make sure that he is getting full value for his money.

Chairman Frank: Is he more careful than usual, then?

Mr. Boyden: I think he is. We are.

Chairman Frank: Then if he is, he won't be hurt?

Mr. Boyden: I think that is true of the sophisticated investor. I don't think it is true of the individual who doesn't have facilities to follow the market carefully.

The high prices resulting from competitive bidding often

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delay distribution and build up security dealer inventories which, when excessive, are apt to create sharp sell-offs and instability in the capital markets.

A second unfortunate development from compulsory competitive bidding might well be the making unavailable to small and medium sized institutions and to individual investors of a still greater proportion of the better grade of new bond issues. Already many of these are denied to institutions like ourselves because of private placement. If competitive bidding should be made mandatory no doubt in many cases the larger institutions would bid directly. Furthermore, in order to reduce distribution expenses investment bankers before bidding might well sound out a group of large buyers as to their interest. In the light of that interest the bankers would figure their bids with the narrowest workable margin in the confident hope that they could place the whole issue with several major buyers at a minimum cost. The result would be that the smaller investors would have to seek other and probably less well secured issues. This method has been used considerably in municipal and equipment financing.

Probably the greatest danger of all from the standpoint of the medium and small sized investors is that competitive bidding would tend virtually to destroy the character of the relationship between the borrower and the investment banker.

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It seems to us that this relationship should be a professional relationship similar to that of client and lawyer or of patient and physician. Probably every well managed corporation has a long range program which involves long range planning. Surely, a continuing relationship between a borrower and his investment banker should result in sounder advice and more constructive results for both borrower and investor than would occur if the borrower should be forced to tell his securities first to one dealer and then another as would necessarily take place with competitive bidding.

Obviously, a borrower-banker relationship would continue only so long as the banker functioned effectively. The banker would be dropped for cause just as individuals change their lawyers and doctors.

A continuing professional borrower-investment banker relationship not only should benefit the borrower but also should be of immeasurable value to the small investor. The investment banker has a dual role. He must provide the capital requirements of his borrower client and he must create sound securities to sell to his customers.

That, certainly, is one of his real obligations. Is it not likely that the professional investment banker serving the borrower over a period of time and intimately familiar with the latter's problems will be a constructive force in setting up sound capital issues?

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The large institutional buyer has his staff of technical experts. The small institution and the individual do not have the facilities for exhaustive investigations of borrowers or their securities. Consequently, it is of great value to those small buyers that a reliable investment banker long familiar with the affairs of the borrower is willing to sponsor that borrower's securities. Can a recommendation carry as much weight to the small investor when it comes from an investment firm, no matter how fine its standards, which is merely the winner in competitive bidding? We don't think so.

Commissioner Pike: One phrase in your statement I hope I misunderstood. Didn't you say that it was the duty of the investment banker to manufacture securities for clients, or did I misunderstand you.

Mr. Boyden: Perhaps I better read it again. The investment banker has a dual role. He must provide the capital requirements of his borrower client and he must create sound securities to sell to his customers.

By that I mean that in taking care of his borrower client's requirements, he must do so in such a way that the securities created are sound.

Commissioner Pike: If you put the emphasis on the "sound." I hope you didn't put it on the factory end.

Mr. Boyden: "Sound" is underscored, Mr. Pike.

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Commissioner Pike: Thank you.

Chairman Frank: Thank you.

Mr. Stewart: Mr. Behrens from St. Louis.

STATEMENT OF ROLAND BEHRENS

ST. LOUIS UNION TRUST COMPANY, ST. LOUIS, MO.

Mr. Behrens: My name is Roland C. Behrens--Behrens.

I am Vice President of the St. Louis Union Trust Company of St. Louis, Missouri. I appear entirely in the role of a consumer or purchaser of bonds. We have never at any time ever participated in the underwriting or selling of securities in 52 years of our history, with which effort I have been identified for almost twenty-four years.

I might explain to the Commission that being interested only in the purchase of securities for trust estates, we naturally have to exercise a high degree of care in that selection and since trust activities today are becoming more and more circumscribed, geographically, by inheritance, estate, and local taxation, we must look very greatly to the small investment dealer in our Community as a matter of good business and public goodwill, and whatever the reasons may be for it in the past few months, we have become increasingly aware of a great concern on the part of the partners of the firms with whom we deal of the effect of competitive bidding on their business.

Be that as it may, they are worried about it. To us, competitive bidding seems undesirable for a number of reasons, some

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of which have been dwelt on already this morning and afternoon. One of the things that is a matter of grave concern to us, as a trust company, is the fact that we frequently purchase securities having the maturity which coincides as nearly as may be with the termination dates of certain trusts.

Under a system of competitive bidding which may develop, of which we can only visualize the results, it is entirely possible that some of the banker-borrower relationships which have developed over a long period of years may no longer be true, if borrowers shop hither and yon and sell their securities to the highest bidder. We are interested because in periods of tight money, less favorable financial conditions than we have by far at present, some of the borrower obligations that we now hold may find it difficult, if not impossible to refund or re-finance those obligations at their state of maturity.

Then, we find ourselves frequently forced to take an enforced refunding because no one will respond to an issue which may not be just the best credit at that time..

Chairman Frank: Is it the experience of the railroads that where the market was adverse, where they sought refundings, that those bankers who sold their securities in good times came forward and assisted them.

Mr. Behrens: I think there <sup>are</sup> one or two instances. One of



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them occurs to me in 1931 on the Frisco Railroad--St. Louis and San Francisco--which had an issue coming due and the bankers did step in the breach and refund those prior lien bonds which were due July 1, 1931, and I think unless there had been a pretty close relationship, I doubt very much if that issue would have been refunded.

Commissioner Pike: Something happened to those bonds later, didn't it?

Mr. Behrens: Right. I mean that is an illustration where I think there was grave doubts about whether it could have been refunded unless there had been some moral obligation, so to speak, which was recognized.

Commissioner Pike: I don't really see who was helped by that.

Mr. Behrens: The fellow that had the bonds was certainly helped because he was paid off.

Commissioner Pike: It shifted the burden somewhat?

Mr. Behrens: Well, that is true.

Commissioner Pike: The fellow that bought the new ones would be in a very fine fix.

Mr. Behrens: From our point of view--we happened to have a few of those bonds--we certainly were relieved at that time and I am afraid today that wouldn't be true. On the question of prices, a lot has been said about the question of the

I think it is very unfavorable--of trust clients with issues that have been sold on a competitive basis of utility bonds in recent years.

As Mr. Fiske indicated this morning, a trustee must invest his money within a very reasonable period of time. And the question of timing judgment, whether it is right or wrong, doesn't enter into it too frequently. It has been our experience that certain issues which have been sold competitively did react downward and, of course, trust clients, while they should not be market minded/<sup>are market minded</sup> today and it has created a feeling of unfavorableness on the part of company trustees and <sup>principals</sup> principles whom we must consult in making investments.

Mr. Healy: Has that ever happened with securities that were issued non-competitively?

Mr. Behrens: Well, I think it is quite true, but, of course, the competitive situation is brought to their attention, and there has been a little tendency, I think, of an attempt in some instances to bid issues up competitively beyond that which a group of investment houses probably would have bid on a negotiated basis. In several of them recently which were ahead of the market considerably.

By that I mean the yield basis would range anywhere from 10 to possibly 35 basis points <sup>ahead of the sale of comparable issues</sup> on the head of the sale of compilations. Of course, it makes it rather difficult

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for a trustee attempting to suggest those bonds for trust clients. Just that difference of opinion, particularly when they have in mind an issue or two prior to that that maybe reacted unfavorably within their memory. Then there is another situation that I think we, as a trustee, must keep in mind, assuming a policy of competitive bidding is adopted.

The margin of profit in which we are, of course, not interested, in any way, may have this effect, which is of indirect interest to us, that smaller firms will place those bonds under the stress of distribution, in accounts where probably the bonds are not entirely suited and eventually as people and as trusts are created we inherit those situations and there seems to be a practical effect, a stigma seems to attach to those issues and when subsequent issues come along I think the investing public keeps those things very definitely in mind.

Commissioner Pike: Any particular group you are referring to there, say, municipals or equipments? There haven't been many utilities in your area.

Mr. Behrens: Well, of course, of direct point the utilities would have to be the only ones. I think, on the investment trust situation in Missouri, we have a rather severe personal property tax, and as a result the recent issues of equipment trust have been priced so that it is very obviously to our advantage not to buy them and

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to buy short term governments or other things because of the tax exemption features.

From the point of view of the bond buyer, the competitive bidding here has taken that group of securities out of our category.

Chairman Frank: Is there a stigma attached to municipal bonds?

Mr. Behrins: I think, as a whole, no, although in many instances, the prices at which some of these municipals have been purchased recently have put us in the position that we get the ones that are offered, that are over-priced, but it is rather difficult to get some of those that are more reasonably priced. I think we have all had that experience.

Commissioner Pike: That is not a difficulty that is inherent in the competitively bought bonds alone. It has been the old story in the investment market.

Mr. Behrens: I grant that point, but the ones, of course, that are of the most vital effect are the ones where the situation has been bid up to the limit, and those are the ones that your clients are more apt to be offered and are able to buy.

The other issues are frequently placed and it is difficult, unless you are in the big money centers, to obtain those bonds.

Another question that bothers us, of course, as I dwelt on a little bit in connection with the refunding, is the fact

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that your competitive bidding idea, of course, at the present time comes up for discussion under one of the most favorable markets from the standpoint of the borrower with lots of money available.

What that condition would be in a condition such as we had in '31, '32, and '33, when your large insurance companies, savings and commercial banks, were on the selling side of securities out of their portfolios, is something that we can only visualize and conjecture upon.

Chairman Frank: And which we scarcely need to consider at the moment because this rule, if it goes into effect is not irrevocable and, more than that, by its very terms, indicates that where it isn't practicable, the rule would be relaxed upon appropriate showing.

So, we needn't discuss a hypothetical situation that doesn't exist.

Mr. Behrens: The only reason I mentioned it, Judge Frank, is that I think a lot of us who have been buying securities -- my experience goes back sixteen years -- we can visualize some of those situations, and as a result, I think it is something that has got to be kept in mind.

If it is adopted it has got to be, as you indicated, that it certainly should be relaxed, <sup>or</sup> left room for modification. Something I can see at that time might have been very serious if it wasn't relaxed promptly. That, in a

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general way, summarizes our feeling, if it isn't relaxed promptly.

Mr. Fournier: In your judgment, are there any investment banking concerns in St. Louis, which are, say, financially competent to head up an underwriting group to handle utility issues?

Mr. Behrens: You mean large issues? I doubt that very much.

Mr. Fournier: Large or small.

Mr. Behrens: It would depend a whole lot upon the size. I can probably only answer that in this fashion, that 1937 in a rather poor bond market--it certainly wasn't the very best -- our Union Electric Company re-financed in June of 1937, put out \$80,000,000 first-mortgage bonds and \$15,000,000 debentures.

I doubt if more than, at the most, \$10,000,000 of those bonds were placed in the immediate St. Louis metropolitan area.

So, when you speak in the terms of "many large issues," I think it is perfectly correct to say that I doubt if there are many houses there, or possibly even a group of the leading houses, that could finance and underwrite such an issue.

When you get down to the issues under \$10,000,000, I think it is distinctly possible they could handle them.

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Mr. Weiner: Do you consider a \$80,000,000 issue to be a sound issue from the standpoint of investor or the company?

Mr. Behrens: I don't think the mere size of it has anything to do with it. I think it is a case of what company and what the set-up is.

Mr. Weiner: What about the maturity of a \$80,000,000 issue? Do you think that is something to look forward to?

Mr. Behrens: Yes, I think it is. I think a \$80,000,000 bond issue, maturing in 1932 and a \$80,000,000 bond issue, maturing today, would present quite different problems.

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Chairman Frank: Of course, one doesn't know, when they are put out, what the situation will be when they mature.

Mr. Behrens: Yes.

Chairman Frank: And the size would make some difference?

Mr. Behrens: To that extent, yes. That refunding and refinancing operation, it definitely would.

Chairman Frank: Thank you very much.

Mr. Stewart: Mr. Charles Engle, Denver, Colorado.