Hon. DAVID I. WALSH,
Senate Office Building, Washington, D. C.

MY DEAR SENATOR WALSH: I am one of the many individuals in Massachusetts serving as a fiduciary for members of my family and others and also serving as a general adviser on business affairs and other matters to members of my family and others in whom I have an interest. In some cases I act as trustee, guardian, or conservator, and in others I act under a power of attorney. I have never held myself out to be an "investment counsel" or "investment adviser," but in connection with the administration of the affairs of those who come to me I have on occasions found it necessary to give advice on the matter of investments.

I receive remuneration for my services on the basis of a fixed percentage of the income at a rate not in excess of the rate generally approved by our courts as reasonable compensation to fiduciaries for services rendered in the continuing administration of an estate. This rate is generally 6 percent of income. The rates charged by reputable investment-counsel firms who are equipped with research organization vary somewhat, but are in general about one-half percent of principal per year. I have never advertised nor have I ever held myself out to be equipped with a research organization or to be an expert on matters of investment.

My attention has been drawn to the definition of the phrase "investment adviser" in title I, section 45, of Senate bill No. 3580, introduced by Senator Wagner and seeking to regulate investment companies. If this definition stands as now worded and the bill is passed, it would require the registration with the Securities and Exchange Commission of myself and many thousands of other individuals in a similar position all over the country unless the Commission should otherwise order. An examination of the bill, of the report of the Securities and Exchange Commission, and of so much of the testimony of witnesses before the Senate Banking and Currency Committee as has come to my attention at this date leads to the conclusion that the primary intent of the bill is to regulate investment companies and investment counsel, so called. I have found no reference to those in my position. Furthermore, under chapter I, section A, of the report of the Securities and Exchange Commission on Investment Counsel filed in connection with this bill, the statement is made:

"As a consequence the Commission did not make the same type of study and investigation of investment counsel services as it did of investment trusts and investment companies. Detailed studies were not made, either through questionnaires or field investigations of individual investment counsel organizations, to ascertain the economic functions performed by or possible defects and abuses existing in these organizations."

It would seem that the comprehensive type of regulation of investment counsel contemplated by the bill under title II should not be attempted without detailed study. Prior to the enactment of such legislation there should be presentation of very convincing testimony to the effect that such regulation would prevent repetition of existing abuses, and would be for the public good.

From examination of some abuses in the investment-company field the Commission has discovered what it considers to be abuses committed by those giving professional advice on investments to others than investment companies. Without a detailed examination of these latter abuses the sponsors of this bill propose regulation not only of so-called investment counsel, but of all others in the country who are engaged in the business of advising others as to the advisability of investing in, purchasing or selling of securities (with certain specific exceptions). Apart from the administrative problem inherent in the registration of so many individuals, an extension of the powers of the Commission into this larger field does not at this time appear to be warranted by the facts or in the public interest.

In the event that Congress should decide that some sort of regulation of investment companies and investment counsel is necessary at this time, I suggest the following wording for title I, section 45 (a) (16):

"'Investment adviser' means any person who advertises, through the press, the mails, or otherwise, that he is engaged in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing or selling securities, and who receives compensation for said advice, or who, for compensation, advises investment companies as defined in this Act as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses of reports concerning securities, but does not include (A) a bank, (B) any lawyer, accountant, engineer, or teacher whose performance of such services is incidental to the practice of his profession, (C) the publisher of any bona fide newspaper or magazine of general circulation, (D) such other persons not within the intent of this paragraph such as the Commission may designate by rules or regulations or order."

This wording varies from the wording as proposed in that with certain specific exceptions it includes under the definition "investment adviser" only those who advertise as such.

If the suggested wording above is for some reason considered inadequate, a possible alternative wording would be as follows:

"'Investment adviser' means any person who, for compensation, is primarily engaged in the business of advising others, either directly or through publication or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses of reports concerning securities, but does not include (A) a bank, (B) any lawyer, trustee, accountant, engineer, or teacher whose performance of such services is incidental to the practice of his profession, (C) the publisher of any bona fide newspaper or magazine of general circulation, (D) such other persons, not within the intent of this paragraph, as the Commission may designate by rules or regulation or order."

This wording varies from the wording as proposed in three respects:

In the second line the original wording is "engages", and has here been changed to "is primarily engaged in".

In the ninth line, (B), the word "trustee" does not appear in the original bill.

In the tenth line the original bill reads, "is solely incidental". The word "solely" has been stricken out.

It would seem that the first of these two suggested alternatives is preferable and that in any case very minor changes in wording, such as suggested above, would be materially less harmful to a large number of individuals who otherwise would become subject to regulation.

Of course, as you know, a trustee, and those who act under a power of attorney in investing funds and do work similar to that of a trustee, here in Massachusetts and in New England, do not advertise for this business, as they more or less follow the same ethics as a lawyer and other professional men, and are considered professional men, but I don't think this is appreciated in other parts of the country.

I am taking the liberty of writing this letter to you, as I do not know Senator Wagner, and I shall greatly appreciate it if you feel that you can pass this information on to him.

With kindest regards, I am

Yours very sincerely,

AUGUSTUS P. LORING, Jr.

RAILWAY & LIGHT SECURITIES CO.,
Boston, Mass., May 1, 1940.

In re: Investment trust bill, S. 3580.

UNITED STATES SENATE,
Committee on Banking and Currency,
Washington, D. C.

GENTLEMEN: Under date of April 19, 1940, I appeared before your committee in objection to the passage of S. 3580. Since that time, there have been submitted, on behalf of a substantial part of the industry, certain constructive proposals which for the most part would remove my specific objections to the bill. There are, however, two matters in these proposals which I believe would represent a source of concern to the stockholders of my company.

1. *Limitations on the issue of senior securities in the future are unnecessarily restrictive.*—Actually the coverage ratio is not significant unless the character of the underlying securities is taken into account. Where high-grade, short-term bonds are held in sufficient amount to cover the debt, only a small margin of such coverage is needed to make the debt safe and prevent the equity being wiped out. Accordingly, any mathematical restriction is likely to be unsuitable for different types of situations, and it would seem that disclosure should be relied on for protection of investors rather than rigid restriction applicable

to all companies. If, however, some mathematical restriction is to be imposed, consideration might be given to the restrictions on loans secured by collateral prescribed by the Federal Reserve Board under the Securities Exchange Act. There were numerous references in the testimony before your committee to these restrictions. I submit that the issue of debt represented by collateral debentures by an investment company is not necessarily more speculative than such collateral borrowings and there is no reason why the restrictions placed on the issue of debt by investment companies should be on a different basis. There are attached as exhibits Regulations "U" and "T" of the Federal Reserve Board now in effect. From these it will be observed that the asset coverage on debt incurred for the purchase of securities must be 166⅔ percent, at the time of the creation thereof.

Any restrictions on the issue of preferred stock should take into consideration the extent to which debt has been issued or is concurrently being issued. For example, in the case of Railway & Light Securities Co., the certificate of incorporation contains a provision that the company shall not issue additional debt and/or preferred stock, if thereby these senior securities will aggregate more than three times the value of the common stock, or in other words, an asset coverage of 133⅓ percent for the combined debt and preferred stock. Without such a dual restriction, the preferred limitation may be of little value. I submit the record of operations of Railway & Light Securities Co. since 1904 (described in my testimony to this committee) as evidence of the efficacy of such a restriction, and likewise as to the sufficiency of the 3 to 1 ratio of senior securities to common capital.

I also feel strongly that great injustice may be done to the interests of investors, if exception to these restrictions is not granted for refundings, reorganizations, and consolidations. These exceptions need be in part only, permitting the issue of debt and/or preferred by the reorganized or consolidated company subject only to the proviso that the asset coverage of the debt and/or preferred stock of the consolidated or reorganized company shall be at least as great as that of its predecessors immediately prior to the reorganization or consolidation.

Dividend restrictions based on an asset coverage are equally illogical because they, too, ignore the character of the assets giving this coverage. In the event that any such restrictions on dividends are placed in the act, they should not interfere with the disbursement of current interest and dividend receipts, provided that the senior capital is not thereby impaired. Furthermore, these restrictions should not infringe existing contract rights.

2. *The prohibition on so-called self-dealing is unnecessarily restrictive.*—I have great difficulty in distinguishing between so-called agency transactions carried out by affiliated persons and purchases from or sales to an affiliated person as principal, provided, however, that such purchases from and sales to affiliated persons are made (a) in marketable securities, (b) at prices not above the then current price, (c) only when the securities are being publicly offered (in the case of a purchase), (d) where the transaction is approved by an independent majority of the board, with prior disclosure of the profit, if any, and (e) where the extent of such profits, if any, are reported to the shareholders at periodic intervals. Such a restriction would adequately safeguard the public against "dumping," would permit the continuance of investment bankers on the boards of investment companies as a minority thereof and would enable the shareholders of investment companies to benefit from the purchase of attractive public offerings sponsored by such investment bankers.

General.—While not bearing directly on the proposals made by representatives of the industry, I would like to mention one further point. An examination of the testimony before your committee reveals several comments made with respect to the inconsistency between the market price and the liquidating values of the common stocks of closed-end investment companies. As a matter of fact, this condition exists at the present time not only with respect to investment companies, but also with practically all of the largest and best known fire-insurance company stocks. A tabulation is attached as an Exhibit A hereto of 10 of the largest and best known fire-insurance companies, running back to 1913, indicating that at the close of 23 of the last 27 years, these stocks were selling in the market at discounts from their liquidating values and often these discounts were substantial. In the balance of the years, you will observe that they sold at premiums and frequently the fluctuations from discount to premium and back again were extremely large. The figures represent an average of these stocks, but each individual one shows the same identical characteristics. The experience of Railway & Light Securities Co. common stock running back to 1904 has been similar. In 23 years out of the last 27 years, it sold at a discount at the year end and in the other 4 years at a premium.

Very truly yours,

RAILWAY & LIGHT SECURITIES CO.,
JAMES H. ORR, *President.*

EXHIBIT A.—*27-year record of percent discount of market price from asset value of common stocks of 10 leading fire insurance companies*

AVERAGE OF 10 FIRE INSURANCE COMPANIES' COMMON STOCKS [1]

Dec. 31, 1913	22.5	Dec. 31, 1928	+35.8
Dec. 31, 1914	22.2	Dec. 31, 1929	+.3
Dec. 31, 1915	23.4	Dec. 31, 1930	9.6
Dec. 31, 1916	26.1	Dec. 31, 1931	22.9
Dec. 31, 1917	29.3	Dec. 31, 1932	22.7
Dec. 31, 1918	38.1	Dec. 31, 1933	20.2
Dec. 31, 1919	26.8	Dec. 31, 1934	7.2
Dec. 31, 1920	28.2	Dec. 31, 1935	+3.1
Dec. 31, 1921	34.7	Dec. 31, 1936	12.2
Dec. 31, 1922	34.2	Dec. 31, 1937	28.3
Dec. 31, 1923	27.8	Dec. 31, 1938	19.6
Dec. 31, 1924	12.2	Dec. 31, 1939	16.2
Dec. 31, 1925	.3		
Dec. 31, 1926	8.3	27-year average	15.6
Dec. 31, 1927	+31.3		

[1] These companies consist of the following: Boston Insurance Co., Continental Insurance Co., Federal Insurance Co., Fidelity-Phenix Insurance Co., Fireman's Fund Insurance Co., Hartford Fire Insurance Co., National Fire Insurance Co. of Hartford, Pacific Fire Insurance Co., Phoenix Insurance Co., and Springfield Fire & Marine Insurance Co.

MAY 1, 1940.

HON. ROBERT F. WAGNER,
Chairman of the Subcommittee of the Committee on Banking and Currency of the United States Senate in Connection with bill S. 3580, Washington, D. C.

DEAR SIR: Although we have not yet had an opportunity to study in detail the framework for an investment company bill, which we understand was suggested to your committee by some representatives of the industry at the hearings last Friday, nevertheless there is one provision as to which we should like to make a further suggestion.

We appreciate the difficulty of drafting any bill to regulate an entire industry which will not result in hardships which may appear unjust to certain parts of the industry. From our hasty examination, it is our belief that the suggested framework as a whole is a most constructive suggestion.

Our purpose in writing this letter is to have on the record this particular point for the consideration of those persons who may undertake the draftsmanship of a bill along the lines of the suggested framework.

Item No. 9 of the suggested framework provides that 40 percent of the directors of an investment company shall be independent of the principal underwriters, regular brokers, managers, or investment advisers. Presumably the purpose of this provision is to insure that the directors are giving their undivided attention to the interests of the shareholders of the investment company and to guard against any possibility of a conflict of interest through the fact that they might be making a profit in some other capacity from the operation of the investment company.

The proposed framework in item No. 14 prohibits self-dealing, as principals, between insiders and investment companies and item No. 21 (e) of the framework requires periodic disclosure of any amounts paid to any director or interested person in the form of indirect compensation. We are entirely in favor of such requirements, having always been opposed to any form of self-dealing by the officers, directors, or trustees of such investment companies. Some investment companies have gone even further than either the suggested framework of the bill or the original S. 3580 and prohibit a director or trustee of an investment company from profiting as a broker, agent or otherwise from transactions with the investment company, involving portfolio securities or other assets of the company.

It is our opinion that where such extreme prohibition is in force the underlying reason for requiring an independent board of directors has been removed. The only interest of directors in such case is to serve the shareholders and under such a set-up it is our opinion that all of the directors are independent in the true sense of the word.

Accordingly, we suggest that there be added to this item No. 9 an exception to the effect that the independent directors be not required in cases of open-end investment companies which by their charters or trust instruments have provided that directors or trustees of investment companies may not, as principals, buy property from, or sell property to, the investment company and also may not, as broker or agent, either directly or indirectly make any profit on transactions with the investment company, involving portfolio securities or other assets of the company.

We also would like to suggest that, in connection with any additional registration required under this act, that where companies have already filed or are currently filing information with the Commission under either the Federal Securities Act or the National Securities Exchange Act, provision be made that a cross reference to such filing and to such information be sufficient rather than require an additional filing of substantially similar information under the proposed act, at considerable trouble and expense to the investment company.

We are making these suggestions applicable only to open-end investment companies because we feel that the redeemable feature gives the shareholder the added protection of being able to take out his money at any time in case he does not like the management or the directors who serve him.

Respectfully,

EATON & HOWARD, INC.,
By W. ELLIOTT PRATT, Jr.,
W. ELLIOTT PRATT, Jr., *Treasurer.*
LOOMIS, SAYLES & CO., INC.,
By MAYNARD HUTCHINSON,
MAYNARD HUTCHINSON, *Treasurer.*

LAW SCHOOL OF HARVARD UNIVERSITY,
Cambridge, Mass., April 27, 1940.

Hon. ROBERT F. WAGNER,
Senate Office Building,
Washington, D. C.

MY DEAR SENATOR: There is one statement in the proposals for revision of Senate bill 3580 presented to your committee by Mr. Arthur H. Bunker which, if correctly reported in the press, ought not to go unchallenged. The statement to which I refer is that the provisions in section 19 of the proposed bill "which interfere drastically with existing contract rights are indefensible." Reasonable men may differ as to the wisdom of some of the provisions in section 19, but it is only beclouding the issue to talk about interference with contract rights. The effect of the section is to limit the power of boards of directors to pay dividends either out of paid-in surplus or out of surplus derived from capital gains. Under existing State laws, no one has a contract right to be paid dividends out of either of these sources. The situation is that the directors may, in their practically uncontrolled discretion, determine whether or not to pay such dividends.

In the case of paid-in surplus, the directors' discretion is even broader. Under the laws of most States, they and they alone determine what if any portion of the consideration which is paid for shares shall be treated as paid-in surplus. If, in the exercise of such discretion, they create paid-in surplus, they then have discretion to retain it in the business or to use all or any portion of it for the payment of dividends. They have in addition discretion to take action at any time which will make such surplus no longer available for dividends by transferring it to capital. In the case of capital gains, the surplus arises automatically if the gains are realized through actual sales of securities, though it is possible that, under the laws of some States, the directors have in addition discretionary power to treat unrealized capital gains—paper profits—as surplus available for dividends. However this may be, they have, with regard to this kind of surplus also, discretion whether to pay it out in dividends, leave it in the business as surplus, or make it permanently unavailable for dividends by capitalizing it.

The issue raised by section 19 is whether the very broad discretion with regard to dividends now given to boards of directors by most of our State statutes is so broad as to be dangerous to the investors' interests, and whether, if such be the case, the particular limitations which section 19 proposes to put upon that discretion are desirable limitations. To call the discretionary power of corporate managers to do as they please with respect to the creation of surplus and its use or nonuse for dividends a contract right of the owners of the enterprise is to invent a wholly fictitious contract for the purpose of seeking to arouse moral indignation based on the wholly unjustified assumption that somebody's contract rights are being destroyed.

I am sending copies of this letter to Mr. Bunker and Mr. Schenker.

Yours sincerely,

E. MERRICK DODD, Jr.

F. EBERSTADT & CO., INC.,
New York, April 29, 1940.

Hon. ROBERT F. WAGNER,
United States Senate, Washington, D. C.

MY DEAR SENATOR WAGNER: Pursuant to arrangements at the termination of the hearings of the Senate Committee on Banking and Currency on the investment trust bill, I would like to submit this letter as a supplement to the record.

On Friday, April 26, Mr. Carlile Bolton-Smith, attorney, general counsel's office, Securities and Exchange Commission, testified with respect to certain transactions which took place about 10 years ago involving Continental Shares and Foreign Utilities, using my name in several instances during the course of his testimony. I think it might be a reasonable inference from this testimony that in some way I determined or shared responsibility for the policies of Continental Shares and Foreign Utilities. While there is no flat statement to this effect in the testimony—the facts undoubtedly having been at the disposal of Mr. Bolton-Smith—through inference that impression is given, and it is wrong. Accordingly, I would like to make this correction for the record.

As Mr. Bolton-Smith states, Continental Shares was organized in 1926. I never even heard of it until shortly before my brief association with Otis & Co. after the market break in October 1929. It is quite evident therefore that I could not possibly have had any participation in its organization, plans, program, or conduct of its affairs prior to October 1929. The same applies to Foreign Utilities.

Subsequent to October 1929, while I was familiar in a general way with the business and policies of Continental Shares, I was never an officer, director, or so far as my recollection and records indicate, even a stockholder, except through my interest in Otis & Co. (which never at any time exceeded 10 percent) in whatever stock of Continental Shares Otis & Co. may from time to time have owned. Thus, I cannot be regarded as having been in control or responsible for the policies of Continental Shares or Foreign Utilities.

Turning to Foreign Utilities, which was also referred to in Mr. Bolton-Smith's testimony, I was never an officer, director, or stockholder in this company. Nor, so far as I know, did Otis & Co. or any of its partners other than C. S. Eaton, occupy any such office or ever own any shares in Foreign Utilities, or have any influence in, or relation with, Foreign Utilities whatsoever excepting a purely brokerage relationship.

There is only one respect in which I may have been said to have exerecised a definite influence with respect to Continental Shares and Foreign Utilities, and that was by my insistence, as a member of Otis & Co., that both of these companies reduce substantially or liquidate the amounts which they, respectively, owed Otis & Co., to which firm I owed sole and undivided allegiance. In negotiating the loan with the Chase Bank, I, being in New York, handled the preliminary conversations upon the initiative and at the request of W. R. Burwell, president of Continental Shares, who subsequently took over the discussions and arrangements.

I would like to emphasize that I am not attempting to explain or apologize for the transactions referred to on the part of Foreign Utilities or Continental Shares; simply that I had no participation, or authority, in these decisions or any responsibility therefor.

Looking back, it is my opinion that the unfortunate results of that situation, in spite of an independent board, were due (1) to self-dealing and (2) to excessive current borrowing. I have attended numerous hearings and read all of the testimony before your committee, and I know of no instance in which anyone from the industry has objected to the definite legal restrictions in the bill banning self-dealing and excessive borrowing.

The fact that Otis & Co. handled issues for certain of the companies, a substantial part of whose stock was owned by Continental Shares, seems to me to be beside the point. I know of no harm, or alleged harm, having come to either Continental Shares or Otis & Co. from this type of transaction.

Quoting from Mr. Bolton-Smith's testimony: "Witnesses have expressed the opinion that if the bill before this committee requires that a majority of the board of an investment trust be independent, there is no need of further restricting the membership of the board." No such suggestion came from me, as can be seen from an examination of my statement before your committee. My suggestion was that not only should a majority be independent of the minority, but that such majority should not be affiliated with each other, which is an additional qualification of very considerable importance, and, in fact, goes further than the terms of the present bill. I never suggested this as a panacea. My remarks, as stated, referred to sections 10 and 11, and it is not to be inferred therefrom that I objected to every other provision in the bill. The above suggestion, taken together with the very proper provisions regarding self-dealing and excessive borrowing, etc., would seem to me to afford complete protection against recurrence of such results as those outlined by Mr. Bolton-Smith.

Sincerely yours,

F. EBERSTADT.

F. EBERSTADT & CO., INC.,
New York, April 26, 1940.

Hon. ROBERT F. WAGNER,
United States Senate, Washington, D. C.

MY DEAR SENATOR WAGNER: Referring to the testimony given before the Senate Banking and Currency Committee on the investment-trust bill at its hearing Thursday, April 25, by Francis T. Greene, Assistant Director, Trading and Exchange Division, Securities and Exchange Commission, I would like to correct what I and others, who have read this testimony, consider distinctly unjust and unfair implications tending to reflect on this firm.

At the outset, if my remarks to the committee in connection with reading the paragraph of Mr. Greene's letter did not make it clear, let me emphasize at this time that the reference to the letter was in no sense intended to reflect in any way on Mr. Greene. From our acquaintance with him we feel very sincerely that he is doing an excellent job. The paragraph was simply read as an example of the extraordinary difficulty which we and others in our business have in complying with the confusing, lengthy, intricate, and complex rules and regulations, in spite of every help and assistance that those on the Securities and Exchange Commission staff endeavor to afford us .

According to Mr. Greene's testimony, this firm "violated the reporting ruling by failing to file any reports showing transactions of the underwriting and stabilizing syndicate, as such, on the day of the offering."

One might fairly conclude from reading Mr. Greene's testimony that we had transgressed, in a willful and substantial way, some rule of the Commission with respect to stabilization, etc. This is not the case and I am sure that Mr. Greene would be the first to substantiate my statement in that connection.

However, he goes on to say that we "should have reported the details of this type of manipulation." I protest against and resent the use of the word "manipulation." Neither in this instance nor in any other, has this firm ever indulged in, or been accused of, manipulation of any sort, form, or manner. There was no question of "manipulation" involved in any way whatsoever and I think the use of that word in reference to this firm was highly improper.

Turning specifically to Mr. Greene's statement that "Eberstadt & Co. violated the reporting rule by failing to file any reports showing the transactions of the underwriting and stabilizing syndicate, as such, on the day of the offering," the facts are as follows:

Pursuant to rule X–17A, we were required over the period from December 7, 1939, to date, to file a total of 136 reports. All of these reports were filed and, so far as I am aware, were filed promptly. On March 21, 1940, it was called to our attention that the very first reports filed were deficient in two respects, namely, that they were filed by ourselves and the other underwriting firm concerned individually instead of being filed by us on behalf of the two firms jointly, and, secondly, that the amount of stock sold by us at retail was not given in the proper form. Both of these alleged deficiencies relate solely to the manner of reporting the facts involved and not to the adequacy of the disclosures of these same facts already made as originally filed. In other words, we, in the course of conducting an entirely legitimate part of our business which, in fact, has been recognized as such by the Securities and Exchange Commission through the promulgation of these very rules, failed to report in the proper manner certain facts which, as a matter of substance, were already fully covered by reports which had been filed promptly and on the day that they were due. Certainly, we feel that this failure on our part is not subject to being criticized as "manipulation" or stigmatized as being the kind of violation which under any possibility could be the subject of "court proceedings."

To Mr. Greene's charge of confusion on our part, I am afraid we must plead guilty.

With respect to the reports in question and with respect to every other statute, rule, or regulation of the Securities and Exchange Commission, our record with the Commission from the time it was originally constituted, is clear and the sincerity of our desire to comply in the most punctilious way with these, to us at least, confusing rules and regulations is only equaled by the generous and cooperative way in which, not only Mr. Greene, but everybody else attached to the Commission, has been of help and assistance to us.

I understand that at the conclusion of the hearings today, those who had testified were to be afforded an opportunity to submit further memoranda. I would therefore greatly appreciate, in justice to this firm, the inclusion of this letter as such in the records of the committee.

Sincerely yours,

F. EBERSTADT.

SECURITIES AND EXCHANGE COMMISSION,
Washington, May 1, 1940.

Hon. ROBERT F. WAGNER,
United States Senate, Washington, D. C.

DEAR SENATOR WAGNER: Mr. F. Eberstadt has been kind enough to send me a copy of his letter to you of April 26, 1940, which he has asked to be included in the record of the hearings on S. 3580.

I do not wish to prolong the discussion as to the character or extent of Eberstadt & Co.'s violation of the Commission's stabilizing reporting rule (rule X–17A–2). Both the original incorrect reports and the corrected reports recently filed by this firm are matters of public record which I should be glad to explain to anyone interested in the details thereof. On the other hand, I should like to make the following comments with respect to some of the points mentioned in Mr. Eberstadt's letter of April 26.

(1) The statement which I made to your committee on April 28, of course, was in no wise intended to be susceptible to any inference that Eberstadt & Co.'s violations were willful. On the contrary, it was my assumption throughout that its violations were the result solely of mistakes—mistakes the recurrence of which I sought to prevent by my explanatory letter.

(2) The firm's failure to file a report covering all transactions by the underwriting and stabilizing syndicate, of which it was the manager, represented, at least in my opinion, a failure to comply with the rule sufficiently substantial in character to justify the detailed explanation made in my letter of March 27. The significance of this violation lay in the fact that the Commission, as a result, was in ignorance of the character or extent of the syndicate's activities on the offering date of the stocks in question.

(3) That stabilization is a form of manipulation is recognized not only by the Securities Exchange Act of 1934 but by the congressional reports recommending the enactment of that legislation. (See, for instance, H. Rept. 1383, 73d Cong., 2d sess., p. 10.)

(4) The failure of Eberstadt & Co. fully to comply with the reporting requirements of rule X–17A–2, of course, did not constitute "manipulation" nor was it so characterized by me.

(5) Insofar as Mr. Eberstadt's letter of April 26 again implies that the rules requiring the reporting of all details of stabilizing operations are "confusing, lengthy, intricate, and complex," I might explain that the risk of injury to the investing public involved in the use of the device of stabilizing is such as to necessitate detailed reports by underwriters as to how they use this device. I might add that the desirability of complete reporting of stabilizing transactions was recognized in a memorandum prepared by Morgan Stanley & Co., Inc., under date of March 24, 1938. In discussing the problem that banking house itself suggested the adoption of stabilizing rules which, among

other things, would require the daily filing by a stabilizer of a detailed report setting forth all purchases and sales made by the syndicate account in the public markets during that day.

If Mr. Eberstadt's letter of April 26 is incorporated in the record, may I request that this reply be also included.

Respectfully,

FRANCIS T. GREENE.

F. EBERSTADT & CO., INC.,
New York, May 3, 1940.

Hon. ROBERT F. WAGNER,
United States Senate, Washington, D. C.

MY DEAR SENATOR WAGNER: Mr. Greene has kindly sent me a copy of his letter to you dated May 1, which he requested be included in the record of the hearings on S. 3580.

I appreciate the spirit of Mr. Greene's letter. It removes the possible unfair and prejudicial inferences which seemed to me inherent in his testimony before your committee, which I felt sure were not intentional on his part.

I would like to close my end of this correspondence by reference to paragraph (5) of Mr. Greene's letter, in which he appears to find endorsement of the present Securities and Exchange Commission stabilizing procedure in a memorandum prepared by Morgan, Stanley & Co., under date of March 24, 1938. I fail to find support for Mr. Greene's point of view in said memorandum. Quoting from the bottom of page 35 of said memorandum: "The two sets of proposed rules on 'pegging, fixing, and stabilizing' which the Commission has prepared and submitted for criticism are so complicated that they would probably never be generally understood, and certainly never be workable," this would seem to me to be exactly what I originally stated to the committee on this subject.

Inasmuch as the previous correspondence on this subject has been included in the record, I would very much appreciate it if you would also include this letter in the record of the hearings on S. 3580.

Sincerely yours,

F. EBERSTADT.

CALVIN BULLOCK.
New York, May 2, 1940.

Re: S. 3580.

Hon. ROBERT F. WAGNER,
Chairman, Senate Banking and Currency Committee,
The United States Senate, Washington, D. C.

MY DEAR SENATOR WAGNER: In the recent hearings of the Senate Banking and Currency Committee on the investment trust bill (S. 3580), quite a number of references were made to the National Association of Securities Dealers, Inc., as a medium through which underwriters and distributors of open-end investment trusts might themselves, under governmental supervision, better solve the regulatory problems involved in the underwriting and distribution of shares of such trusts than such problems could be solved through the mechanism contemplated in S. 3580.

In the course of these hearings, and in connection with these references to the National Association of Securities Dealers, Inc., there were several questions about the association which led me to believe that it might be helpful to the committee to have before it, in its consideration of this bill, a descriptive statement concerning the association, its background, its legal relationship to the Securities and Exchange Commission, its objects, powers, nature, method of operation, and state of development at the present time. I am, accordingly, addressing this letter to you with that end in mind; and I earnestly request that it be made a part of the record of the hearings for that purpose.

The National Association of Securities Dealers, Inc., is registered with the Securities and Exchange Commission as a national securities association pursuant to the provisions of section 15A of the Securities Exchange Act of 1934, as amended.