

conditions the amount of stock is not quite as important as it has been under the old set-up.

Mr. BOREN. All right.

Mr. HEALY. On your \$100,000-point, on the limitation, we have got some limitations in here on the issuance of senior securities by companies which are not face-amount companies, that is, in ordinary investment-trust corporations. They cannot issue debt securities; that is, debentures or bonds and notes, unless they have assets covering them 300 percent. They cannot issue preferred stock unless they have assets covering it of 200 percent. That kind of a provision is just as good or even better than one that would require that you could not issue evidences of indebtedness until you had so much subscribed capital stock. As a matter of fact, it seems to me that would be the way it would work out; that you could not issue debentures or notes unless you have a 300-percent coverage.

Mr. BOREN. Assuming that the bill does, in the provision you have indicated, take care of the problem I have in mind, referring again to the \$100,000 and your method of arriving at that arbitrary figure—would not that figure in some instances be inadequate for the purpose in mind and in other instances prevent very small operators, we will say a given company which in every other respect may be sound?

Mr. HEALY. Well, you do not want to have people starting these companies on shoestrings? Do you want a lot of adventurers that go out and get the public's savings? What you say would have a great deal more appeal to me, were it not for the fact that there has already been written into this bill this requirement for the maintenance of ratios of assets to senior securities. The company cannot issue debentures except where they have a 300 percent asset coverage. Do you not think that that meets your point?

Mr. BOREN. Right at that point, though, if the safeguards which you point out are sufficient to meet the problem I had in mind, what difference does it make whether the company starts out with \$500,000 or \$5,000 if the actual money provided for every certificate it sells has a satisfactory guarantee behind it, or whether you start out with \$5,000,000?

Mr. HEALY. I think these enterprises should not be started and then promoters permitted to go out and solicit the public's money unless there is really something substantial back of them and a basis for starting the enterprise.

You do not want these things to be wildly speculative.

Mr. BOREN. Finally, then, I take it that this figure was arrived at somewhat arbitrarily with the theory that if less than this amount of money were invested they would be unable to maintain their overhead, operating costs, and similar contingencies.

Mr. HEALY. I am perfectly willing to agree that the figure was arrived at somewhat arbitrarily. Any safeguard of this sort has a certain amount of arbitrariness in it. That is, you cannot find an absolute standard to measure the figure by. The basic idea and the consideration that influenced me in supporting that recommendation, was the feeling that if promoters can not get \$100,000 together, they should not be allowed to go out and solicit the custody and management of the public's funds in a fiduciary capacity.

Mr. BOREN. That figure must have been surely based upon the feeling that any amount of money less than that would be a sum

which was too small to produce the necessary overhead and operating expenses of a minimum company.

Mr. HEALY. That is true.

Mr. BOREN. Just one other question on this point and I will pass.

I want to understand what has been done in some instances, or what can be done, we will say, with this \$200, assuming that this \$200 was paid in and this certificate had lapsed, and the contract becomes void and, of course, worthless.

Now, the \$200 put in here, I presume, then goes into the general funds of the corporation and can be disbursed as dividends to the stockholders; is that correct?

Mr. SCHENKER. Most of it, Congressman, is used to pay the salesman to go out and get the prospect. Selling contracts on installment plans requires concentrated sales effort, and a good deal of that \$200 goes into the general fund of the company, which can be disbursed for any purpose of the company. The major part of it goes to the salesman, for overhead and operating, and if there is any portion left it goes to dividends on the common stock. Under the new bill which is proposed, that situation could no longer exist. We have made it so that the sale load is more equitably distributed over the life of the contract, and we have a proviso here so that a person who goes into this type of an institution must get at least 50 percent of his money back the first year, and he starts getting surrender value at the end of 4 months rather than at the end of 2 years.

Mr. BOREN. Or the third year?

Mr. SCHENKER. Or the end of the third year in some cases.

Mr. BOREN. Mr. Chairman, I would like to request that Commissioner Healy or some of his assistants take this contract that I referred to, which, as I said, is a certificate sold to a school teacher in Oklahoma, and examine this certificate, showing what this bill will do to this certificate, by way of an analysis of the conditions thereof.

Mr. HEALY. We will be very glad to do that, Mr. Boren.

Mr. BOREN. I would like to have that done.

Mr. HEALY. We will be glad to do it.

Mr. COLE. Gentlemen, the committee wants to use this room immediately for an executive session, so we will recess until 2 o'clock this afternoon.

(Thereupon, at 11:45 a. m., a recess was taken until 2 p. m. of the same day.)

AFTERNOON SESSION

The subcommittee reassembled, pursuant to the taking of the recess, at 2 p. m., Hon. William P. Cole, Jr. (chairman) presiding.

Mr. COLE. The subcommittee will come to order, please. I am sorry that the subcommittee is so late in convening, but we have to take that chance in holding hearings in the afternoon, especially at this time, when there is so much important business on the floor. The bells may ring at any time.

I have a list before me of the gentlemen whom I assume are here. Judge Healy, do you want to present the gentlemen on this list, or shall I just call them?

Mr. HEALY. I think you might call them, Mr. Chairman.

Mr. COLE. Mr. Arthur H. Bunker is the first one on the list. We will be glad to have any statement you care to make at this time, Mr.

Bunker. Identify your committee, and state what you think of this bill, and why.

STATEMENT OF ARTHUR H. BUNKER, EXECUTIVE VICE PRESIDENT, LEHMAN CORPORATION, NEW YORK, N. Y.

Mr. BUNKER. My name is Arthur H. Bunker. I am executive vice president of the Lehman Corporation of New York City, and am chairman of a group who have been representing informally a substantial part of the closed-end investment companies in connection with the bill before this subcommittee.

Mr. Ranald Macdonald of National Bond and Share Corporation, Mr. Raymond McGrath of General American Investors Co., Inc., and Mr. Cyril Quinn of Tri-Continental Corporation and its affiliated companies, who are here with me today, are members of this group. Mr. Alfred Jaretzki, Jr., of Sullivan and Cromwell, has been acting as our counsel.

Our group appeared before the Senate subcommittee at its hearings on the original bill. We objected strenuously to a number of the provisions of that bill, but expressed ourselves as favorable to reasonable regulation of investment companies.

At the close of the hearings I submitted concrete proposals for legislation which had been worked out by my group, in conjunction with the leading representatives of the open-end companies. Thereafter, with the approval of the Senate subcommittee, representatives of both the closed-end and open-end investment companies cooperated with Judge Healy and Mr. Schenker of the Securities and Exchange Commission in an endeavor to agree on principles for regulation which we might be able to recommend jointly to the Congress. In this we were successful and a memorandum of principles was prepared embodying this agreement.

This memorandum was then circulated among representatives of all the investment companies who had appeared at the Senate hearings, and a great many others, constituting a very substantial portion of the industry.

This agreement received unanimous endorsement of the industry.

Mr. COLE. Have you a copy of that paper with you?

Mr. BUNKER. Yes, sir; or we can furnish a copy. I do not have one here.

Mr. COLE. What is the date of it?

Mr. BUNKER. The date must have been about five weeks ago; May 13, 1940.

Mr. COLE. Let me understand that again. So far as title I is concerned, after your group got together and prepared a memorandum which went out to all of the industry throughout the United States and they had ample opportunity to study it?

Mr. BUNKER. Yes, sir.

Mr. COLE. And to report back to you before the Senate committee acted?

Mr. BUNKER. Yes, sir; what we really did was at the last day of the hearings, which I believe was the last Friday in April—we were concerned with title I only—we submitted a series of suggestions embodying principles, and those were principles to which the industry was agreeable. They had not theretofore been submitted to the Securities and

Exchange Commission. They were the industry's idea as to what was necessary and adequate. Immediately succeeding that, at the request of the subcommittee, the industry's representatives got together with the Securities and Exchange Commission and evolved the principles which were jointly acceptable to both the industry and the Securities and Exchange Commission. That agreement was first circulated, and was only a memorandum of principles, and in no sense reduced to the language of a bill.

So, the first step was that these general principles received the unanimous support of all who had been present in the hearings and a great many others as well—in my opinion, the preponderant group of the industry. I think some 58 major companies were involved in that.

After that agreement of principles had been approved by the industry and the Securities and Exchange Commission, Mr. Jaretzki, representing the closed-end companies, and Mr. Warren Motley of Boston, representing the open-end companies, collaborated with Judge Healy, Mr. Schenker, and the staff of the Securities and Exchange Commission, in reducing these principles to the language of a bill, and the bill as drafted was again circulated among the industry, because, of course, at that time the representatives of the industry units were scattered home again. They had all been assembled here. These principles again received the unanimous approval of the industry in the form of the bill which is now before you.

Since it has had that joint approval, we are naturally interested and accordingly we strongly urge its passage at the present session. We believe this to be a workable bill and a bill which will be beneficial to the industry. We recognize that abuses have existed in the industry and we feel that legislation is necessary to prevent their continuance and to help the better elements of the industry to raise the standards of the industry to increasingly higher levels.

Since the investigation of investment companies was commenced 4 years ago, the industry has been living under the cloud of investigation and under the threat of legislation whose character could not be known. With this bill passed, we will know where we stand and we will be able to make our plans accordingly.

We trust that the present national emergency should not be a deterrent to its enactment but should rather serve as an added reason for the passage of the bill.

We feel that it is a very healthy sign that the Government and industry can come together and do a constructive job of this character.

With this legislation the confidence of the public in investment companies will, we believe, be restored, and these companies will be able to serve not only the investor but also the important function of supplying new capital to those industries vital to the national defense.

In closing, may I just add a word of appreciation of the splendid cooperation which our group has received from the Securities and Exchange Commission. I think it is a real achievement, which both we and the Commission can feel proud of, that we have been able to cooperate so effectively and work in such close harmony in the development of these proposals for legislation. And, I think it is only fair to say, that this would not have been possible had it not been for the complete spirit of fairness on the part of Judge Healy and Mr. Schenker in dealing with us and these problems.

Mr. BOREN. Mr. Chairman.

Mr. COLE. Mr. Bunker, I have had presented to me by one of my colleagues of the House suggestions of a constituent of his embodying two suggested amendments: One is to add subsection (c) to section 20, dealing with proxies, voting trusts, and circular ownership, and the other expressing opposition to section 37, dealing with larceny and embezzlement, on page 139 of the bill, I think it is. Will you look at the language of this amendment and state for the record whether this matter was before your group at the time you agreed upon it?

Mr. BUNKER. Whether this particular amendment was before our group?

Mr. COLE. Yes.

Mr. BUNKER. Yes; I will be glad to.

Mr. COLE. Who is this gentleman with you?

Mr. BUNKER. Mr. Jaretzki, our counsel.

Mr. JARETZKI. Is that agreeable?

Mr. COLE. Perfectly; I just wanted to know who you are.

Mr. BUNKER. Mr. Cole, Mr. Jaretzki knows all about this. Frankly I know nothing about circular ownership. It has never interested me, and Mr. Jaretzki has been down here during the last 3 weeks cooperating in the drafting of this proposed bill, and if it is agreeable I think that Mr. Jaretzki could give you a more competent answer.

Mr. COLE. Mr. Jaretzki, are you going to testify later?

Mr. JARETZKI. Yes, sir.

Mr. COLE. Suppose that we just hold this, then, until that time. I want to clear it up.

Mr. JARETZKI. Yes, sir.

Mr. COLE. That is all, Mr. Bunker?

Mr. BUNKER. Yes, sir.

Mr. COLE. All right, Mr. Bunker, we thank you. You are going to give me a copy of the agreement?

Mr. BUNKER. Yes, sir; that is the May 13 agreement of principles.

Mr. COLE. Yes.

Mr. BUNKER. That is the only thing that you have asked for, is it not?

Mr. COLE. Yes. I would like to have the original which went out to the industry.

Mr. BUNKER. Yes, sir. That was the May 13 agreement of principles.

Mr. COLE. Very well.

Mr. BUNKER. Yes, sir. Thank you. I will see that you get one. (Memorandum referred to appears in the hearings of June 14, 1940.)

Mr. COLE. Mr. Quinn.

**STATEMENT OF CYRIL QUINN, VICE PRESIDENT AND DIRECTOR
OF TRICONTINENTAL CORPORATION, NEW YORK, N. Y.**

Mr. QUINN. Mr. Chairman, my name is Cyril Quinn. I am a vice president and director of the Tri-Continental Corporation and of the four investment companies that are associated with it. My address is New York City.

I would like to second what Mr. Bunker has said and I would like to add this word. During the hearings before the Senate committee

I appeared as one of Mr. Bunker's group, representing the closed-end companies. I appeared in opposition to certain sections of the bill and discussed in some detail the various technical provisions of some of it.

I would like to say that the bill now before you, in my opinion, is a good bill. It is a workable bill in that the rules under which the industry will have to operate are clear and explicit, which I think is a requirement of any proper regulatory bill. I think it is a reasonable bill in that, while it sets up certain safeguards, it still leaves the management freedom of action in meeting the responsibility of handling the funds that are entrusted to it. I think also that it will be an effective bill in that certain practices in the past which have existed are safeguarded against, and certain desirable practices which many companies are now following are now required of all companies.

Therefore, I would like to make clear to you, sir, my support of the bill as it stands at the present time.

Mr. COLE. Where is your office?

Mr. QUINN. New York City, sir.

Mr. COLE. All right, sir.

Mr. QUINN. Thank you.

Mr. COLE. Mr. Raymond McGrath. Is Mr. McGrath here?

Mr. BUNKER. I think that Mr. McGrath is not here just at the moment, Mr. Chairman.

Mr. COLE. Mr. Bellamy, of the National Bond & Share Corporation.

Mr. BUNKER. Mr. Bellamy is not present. He represents the National Bond & Share. Mr. Macdonald is present.

**STATEMENT OF RANALD H. MACDONALD, VICE PRESIDENT AND
DIRECTOR OF THE NATIONAL BOND & SHARE CORPORATION,
NEW YORK, N. Y.**

Mr. MACDONALD. My name is Ranald Macdonald. I am a vice president and director of the National Bond & Share Corporation.

Mr. COLE. Of New York?

Mr. MACDONALD. New York. It is a smaller investment company, with assets between \$7,000,000 and \$8,000,000, and its directors are members of the firm of Dominick & Dominick.

Our company is a closed-end company. Its stock is listed on the New York Stock Exchange and it has only one type of stock outstanding—common stock.

The statement that we have to make on this bill, as it stands now, is very short; merely to the effect that we believe that this bill is entirely workable as it is now drawn and we believe that the bill should be passed, and hope that it will be passed.

Mr. COLE. Are you the Mr. Macdonald referred to in a letter addressed to me under yesterday's date over the signature of Mr. Starkweather, chairman, Federal legislation committee of the Investment Bankers Association?

Mr. MACDONALD. I am.

Mr. COLE. I asked Mr. Starkweather if he wanted to appear at the hearings today or tomorrow and he wrote me this letter which I will insert in the hearings at this point.

(The letter referred to is as follows:)

INVESTMENT BANKERS ASSOCIATION OF AMERICA,
New York, June 12, 1940.

The Honorable WILLIAM P. COLE, Jr.,
New House Office Building, Washington, D. C.

DEAR MR. COLE: Thank you for your letter of the 11th, advising me that hearings on the investment trust bill, S. 4018, will be held before your subcommittee on Thursday morning, June 13.

As I advised you over the telephone, the Investment Bankers Association has followed the investment trust legislation with great care and was prepared to testify before the Senate Committee on Banking and Currency. However, by the time these hearings had progressed for a few days it became apparent that substantial changes would have to be made and in view, also, of the very complete case presented by the investment trust business itself, we decided not to introduce testimony at that time.

Since that time we understand that a complete agreement has been reached on a new bill, which presumably is the one referred to in your letter, between the Securities and Exchange Commission and the committee representing the investment trust business. The committee of this association which follows investment trust matters has been in constant touch with the progress of these negotiations and is in entire accord with the results reached.

Mr. Ranald H. Macdonald, chairman of our investment companies' committee, will be in Washington for the hearings tomorrow morning and will, no doubt, be in touch with you.

Very truly yours,

JOHN K. STARKWEATHER,
Chairman, Federal Legislation Committee.

Mr. COLE. All right, Mr. Macdonald, is that all?

Mr. MACDONALD. Yes, sir.

Mr. COLE. I see that the letter supports the bill.

Mr. MACDONALD. This letter supports the bill, and while we have not had a formal meeting of our entire committee, due to the fact that the members are located in different parts of the United States, I have had enough information about the opinions of various members of the committee; members of the board of governors, and members of the association, to feel that they are in accord with the opinion that I have just expressed in behalf of the National Bond & Share Corporation and favor the passage of this bill.

Mr. COLE. I wrote to Mr. Starkweather, because I saw quite a lot of him last year during the consideration of the indenture bill.

Mr. MACDONALD. Yes, sir; I know that.

Mr. COLE. And he asked to be notified about this. I hope I have not overlooked anyone whose name was in my files, as wanting notice of the hearing.

Mr. MACDONALD. Mr. Starkweather is chairman of the Federal legislation committee of the Investment Bankers Association.

Mr. COLE. Yes. Is that all?

Mr. MACDONALD. Yes, sir.

Mr. COLE. All right, sir. Thank you.

Mr. MACDONALD. Thank you.

Mr. COLE. Mr. McGrath.

Mr. BUNKER. He is not here, and I will speak for him. He has asked me to speak for him to the extent of saying that the bill has his wholehearted endorsement.

Mr. COLE. That is, Mr. Raymond McGrath, General American Investors Co., Inc.?

Mr. BUNKER. That is right. He has authorized me to speak for him. I am very familiar with his idea, right up to the last minute, and his opinions.

Mr. COLE. Now, we have the open-end company group. I will take you gentlemen in any order you wish to appear.

STATEMENT OF PAUL CABOT, REPRESENTING STATE STREET INVESTMENT CORPORATION, BOSTON, MASS.

Mr. CABOT. My name is Paul C. Cabot, and I am one of the organizers and vice president of the State Street Investment Corporation of Boston, which we started in 1924.

The original bill as it was presented to the Senate did not, except in one minor instance, affect the operations of my particular company. I felt, therefore, that I was in the position of being at least unbiased in criticizing that bill; but I felt very strongly that the bill as originally drawn would be a mistake for the industry and the people in general.

The present revised bill which you have before you, I think is an excellent one, and I am heartily in favor of it.

In the past there have been a great many abuses that have been brought to your attention by the reports of the Securities and Exchange Commission.

It is my considered opinion that this bill will eliminate, or at least largely mitigate, those abuses that have been present in the past and I hope that you will act favorably upon it.

Mr. COLE. All right, sir.

STATEMENT OF WILLIAM TUDOR GARDINER, REPRESENTING INCORPORATED INVESTORS, BOSTON, MASS.

Mr. GARDINER. Mr. Chairman, my name is William Tudor Gardiner, chairman of Incorporated Investors, an open-end, management-type company in Boston, with redeemable shares and assets of around \$40,000,000.

Mr. COLE. You are former Governor Gardiner.

Mr. GARDINER. Yes, sir. I would like to say a word about the need for this type of legislation.

The more consideration I gave to the matter, the more important it seemed to me that there should be some such legislation as this.

Essentially, the investment-company industry involves the gathering together of cash and negotiable securities for management, and that facilitates a wrongful use if management falls into unscrupulous hands; if the managers are dishonest, unscrupulous, or even selfish, there can come great harm to the stockholders.

As to the form of this legislation, I must confess that at one time it appeared to me desirable if a simpler bill could be produced, but careful study satisfied me that the task can in no way be further simplified than it has been done in this bill.

The legislation must cover a great variety of investment companies, and that is one of the reasons for the length of this bill.

As some of the questions by the chairman, Mr. Cole, this morning indicated, publicity is a great regulating force; but in the case of complex corporate structures and practices, I think it is plain that publicity is not enough.

This bill, I believe, covers the situation adequately, and without undue restriction on legitimate business.

I would like to urge upon the committee the fact that many man-hours of work have gone into this piece of legislation. It has been a great demand on the time of many representatives of this industry.

We most earnestly hope that this matter will have your prompt consideration and that the action of the Congress may be favorable, so that the industry can carry on its other work.

Mr. COLE. Governor, it pleases me, as well as the rest of the committee, to hear statements such as we have heard here this morning, and to find an important industry like this and the Securities and Exchange Commission getting together as they have. It is a highly technical piece of legislation. This committee likes to see such results as this bill presents. There was a day when the industry did not think they could approach, let alone try to get together with the Securities and Exchange Commission, but during the last year or two they have been finding that they are human, just like the rest of us, and trying to do a good job. If I thought the Securities and Exchange Commission deserved the criticism we hear from some sources I would not be a party to trusting it with the important and new jurisdiction this bill confers.

Mr. GARDINER. That is true, Congressman, and I would like to add to that that the extensive studies carried on on the subject by the Commission were very helpful in collecting information about this industry that is scattered throughout the country, and a great many of us worked with the Commission in that study.

Mr. COLE. All right, sir. Thank you.

Mr. GARDINER. Thank you.

STATEMENT OF MAHLON E. TRAYLOR, PRESIDENT OF MASSACHUSETTS DISTRIBUTORS, INC., BOSTON, MASS.

Mr. COLE. We will hear Mr. Traylor.

Mr. TRAYLOR. Mr. Chairman, my name is Mahlon E. Traylor. I am president of the Massachusetts Distributors, Inc., of Boston, the sponsor company for Massachusetts Investors Trust, Supervised Shares Inc., and Boston Fund, Inc. These are funds with assets aggregating more than \$100,000,000.

Mr. COLE. Why is it that all of the open-end companies apparently come from Boston; is there something peculiar about that section of the country that accounts for that?

Mr. TRAYLOR. The open-end industry started in Boston, Mr. Cole. I want to mention one or two points.

Mr. COLE. Are they confined now to that section of the country?

Mr. TRAYLOR. No, there are open-end companies, a number of them in New York; one or two in Chicago, and one or two on the coast, and a number in Boston.

Mr. COLE. Mr. Traylor, I am going to have to ask you to suspend again for a few minutes in order that we may answer a call of the House.

Mr. TRAYLOR. May I just go on record as saying that I endorse this bill.

Mr. COLE. Is that all you had to say?

Mr. TRAYLOR. I was going to mention a few points in connection with the selling end, but it is not necessary to mention them in detail.