

MEMORANDUM . . . CHAIRMAN . . . FIVE

DATE February 1, 1937

TO: Chairman Landis

FROM: Allen E. Throop

SUBJECT: Registration Statement for Konversionsklasse I - 1937
Memorandum by Mr. Hawes

Please note the attached memorandum of Mr. Hawes, concurred in by Mr. Bane, with reference to the Conversion Office's registration statement.

Commissioner Douglas conferred with Mr. Reuben Clark and me when Reuben Clark was here on Wednesday, and I left with the Commissioner a copy of Mr. Greene's proposed release. Sam Clark has revised it to incorporate some of the Commissioner's suggestions and Mr. Greene and I are to discuss it shortly with Mr. Clark. I will let you know as soon as we have done so. In the meantime, you may wish to give consideration to Mr. Hawes's memorandum.

Attachment

MEMORANDUM TO MR. THROOP:

Re: Registration Statement for
Konversionskasse

I have read the January 26 draft of the proposed release on this statement and a copy of the bulletin referred to in the release. I had not previously realized the weakness of the position which the Commission proposes to take. I think that the release certainly emphasizes that.

I am more than ever convinced that the Commission should not permit the statement to become effective without the inclusion of some statement concerning the amount of the unrecorded debt. I trust that there is no idea of accelerating the effectiveness of the statement and thereby implicitly recording the satisfaction of the Commission with the statement as it stands.

Aside from the foreign exchange situation, of a foreign government, nothing seems to me more important than its indebtedness. While internal indebtedness of a foreign government may not be of great importance when it is a reasonable amount, it becomes of tremendous importance when it indicates the possibility of the bankruptcy of that government. It is certainly the general impression that the German government is very rapidly approaching the danger of bankruptcy, which will actually threaten the continued existence of the present government. Some such reasoning is undoubtedly the basis for the decision of the Commission to release a statement concerning this unrecorded debt. The release asserts that security holders to whom this offer is to be made and subsequent purchasers should be informed of this body of unrecorded debt regardless of whether it constitutes "indebtedness of the German government".

If this is so, it is because this unrecorded debt is a material fact, and it would seem to be a material

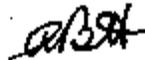
fact necessary to make the remaining statements in the registration statement not misleading. The Commission therefore has a clear duty to require its inclusion in the registration statement. It cannot discharge this duty under the Securities Act by getting out its own release. While the release states that "in order to fulfill this paramount purpose of the Securities Act of 1933, the Commission considers it necessary that full publicity be given to the existence of the 'unrecorded' 'future short-term obligations' of the Reich", the full publicity contemplated by the Act is that which results from inclusion in the registration statement and reflection in the prospectus.

Moreover, having been put on notice of the amount of this unrecorded debt existing on June 30, 1935, and with the knowledge of the history of Europe during the past eighteen months which the ordinary newspaper reader has, it seems to me that the Commission is under an obligation to attempt to discover the amount of the unrecorded indebtedness as of a recent date. The fact that such figures have not been published by the German government is no justification, in my opinion, for failing to require their disclosure at this time.

Not only do I think that the Commission would be remiss in its duty in failing to require these disclosures in the registration statement, but I also believe that it would be made the subject of a great deal of adverse criticism. The German government's position is widely known or suspected at the present time, and there is a great deal of interest in it, because of Germany's extensive rearmament program. Numerous articles have appeared in American magazines in the past four or five months on this very subject. Consequently I do not think that the Commission's action will go without notice.

It seems to me that it will be difficult to justify this action on the ground that the Commission does not wish to prevent American holders of German securities from enjoying the benefits of the proposed offering. Unlike the previous offerings, there is no provision here for redemption of the new bonds in

American currency. The holder can secure for his bonds a percentage of their face value only in German marks, which of course cannot be used for the purchase of foreign exchange. The offering therefore involves merely the exchange of pieces of paper. While it does also involve the recognition of this indebtedness by the German government, I seriously question the value of this recognition in view of Germany's history of defaults and the relative instability of the present government. In any event it seems to me that whatever additional benefit will accrue from this recognition, it is insufficient to outweigh the disadvantages of the proposed action.



Alexander B. Hawes

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January 29, 1937

