the operating records of the smaller trusts. Moreover, open-end funds are not trading companies seeking short-term speculative profits. They are vehicles for conservative, long-term investment.

A study of the comparative performance of the 22 open-end trusts just referred to for the 3-year period January 1, 1937, to January 1, 1940, shows that only one of these companies had a better investment performance than did the largest company in the field (based on liquidating values as of the two dates, with adjustment for dividends paid). Although the companies used in this comparison were representative, there may have been a few other companies whose performance was better.

Since this period covered a representative market cycle from high to low and with a partial recovery, it affords clear proof that the size of the Massachusetts Investors Trust portfolio placed it at no disadvantage as compared with smaller trusts.

Our trust has experienced no difficulty in buying and selling securities promptly and in orderly fashion. In the first place, total assets of a trust do not necessarily determine the size of its individual holdings. A number of trusts that are smaller hold larger blocks of certain individual issues. With minor exceptions, no block of stock held by Massachusetts Investors Trust represents as much as 4 percent of the issue in question; and holdings, in the average, represent less than one-half of 1 percent of the issues in question.

Massachusetts Investors Trust holds 115 separate issues, giving far greater diversification than most other trusts; and because of its over-all size, it can afford the research and other facilities necessary to supervise that number of issues. Moreover, further growth of the trust would not necessarily require any increase in the size of individual holdings, because out of the 2,200 stock issues available on the New York Stock Exchange and the New York Curb Exchange, there are many more than the 115 issues now held that would make suitable investments.

In connection with ability to liquidate holdings when necessary, it is important to remember that virtually all issues held enjoy active markets. In this respect, an open-end trust is in a much better position to realize on its assets promptly and at fair value than is a life-insurance company or a savings bank of the same or larger size, whose assets are in far less liquid securities in many cases.

There are many trust companies and certain investment advisory organizations throughout the country which supervise investments in amounts much larger than any investment trust now in existence. When such investment advisers and trust companies recommend sale of a specific security, the resulting selling orders may come simultaneously into the market in haphazard fashion from perhaps 100 or more different investors. Since this condition is apparently not a matter of concern, it is difficult to see why it should be in the case of an investment fund such as Massachusetts Investors Trust, where selling is orderly and controlled because it comes from a single source.

Like every other type of financial institution that permits withdrawals, the maximum size of open-end funds will be determined naturally by economic considerations. As the size of an open-end fund increases, the normal volume of liquidation by shareholders also increases. Thus, the excess of the volume of shares sold, over the volume redeemed, declines steadily, and the size of the trust is

limited at the point where sales finally do no more than off-set redemptions.

So convinced were our trustees of the inevitable course of this trend that 2 years ago they set a limit of 6,000,000 shares on the capitalization of the trust. The shares sell for about $20 apiece.

This was no tacit admission that a trust of larger size was cumbersome or undesirable. It represented merely a practical recognition of the difficulties of increasing assets beyond that point. Experience of the past 2 years shows that this expected balance between sales and redemptions is rapidly developing. The following figures clearly show the trend:

In 1937, 1938, and 1939 the dollar volume of shares sold was, respectively, as follows: 1937, $26,314,000; 1938, $14,384,000; 1939, $11,805,000.

In those same years the amount redeemed was, in 1937, $7,025,000; 1938, $7,883,000; 1939, $8,216,000.

In other words, we have approached the point in the last 2 years where our redemptions approximately equal our new sales.

Senator HUGHES (presiding). State that again, will you please, with reference to your redemptions?

Mr. GRISWOLD. Let me put it this way. Our redemptions are fairly constant. They are about 8 percent of our fund per annum. For example, in 1937 we paid back $7,000,000; in 1938 we paid back $7,800,000; in 1939 we paid back $8,200,000.

We have now reached a point where our new sales are approximately equal to that, or where these figures approximately equal our new shares. In other words, an open-end trust could never be a billion dollar company or a five hundred million dollar company, because redemptions, which are a fixed percentage, around 8 or 10 percent, get to be so large, when your fund gets to those big proportions, that you could not resell that amount of shares; and we therefore claim that economic conditions absolutely take care of this situation, and that there never will be an open-end investment trust with assets like life insurance companies and large banks.

Senator HUGHES. Thank you.

Mr. GRISWOLD. I will now deal with the social aspects. Even though large size results in no operating inefficiency or penalty to shareholders, we realize that big aggregations of capital funds must also be examined in the light of their social significance and from the standpoint of possibly undesirable concentration of control over the country's business and industry.

Will you pardon me, Senator? I omitted a small part of what I wanted to say. After reciting those statistics I should like to summarize and say the following:

We submit that the foregoing facts indicate that—

1. Large size reduces the investor's costs.
2. Arbitrary reduction or limitation of size will increase the investor's costs.
3. There are no serious operating or market problems involved in managing a large investment fund.
4. Size is no handicap to investment performance.
5. Economic factors will automatically limit the size of any mutual fund.

Senator DOWNEY. Mr. Chairman, I have to withdraw now, and I regret it very much. I shall read your testimony, Mr. Griswold.

(Senator Downey withdrew from the hearing room.)

Mr. GRISWOLD. Regarding this argument of undesirable concentration of control, we wish to point out that the basic theory of the mutual fund prevents any such fund from acquiring control of any business. Quite the contrary, such trusts do not invest more than 5 percent of their funds in the securities of any one company, and can invest in no more than 10 percent of the outstanding securities of any one company.

That is equally true of all diversified funds, closed or open. That is true today of the open-end trusts.

As a practical matter, Massachusetts Investors Trust has diversified its investments even more than required by these provisions. It has less than 4 percent of its funds invested in the securities of any one company, and its 10 largest individual holdings, in the average, represent less than four-tenths of 1 percent of the outstanding securities of the corporations in question.

It should be obvious, from the foregoing discussion, that Massachusetts Investors Trust does not desire, and in fact cannot use, its funds to subject corporations to its control or influence.

If it is feared that a group of open-end trusts under the same management might conceivably obtain control of other corporations through their combined holdings—this I should like to say is one of Mr. Frank's ideas—any such possibility can easily be prevented without arbitrarily limiting even the size of the group. For instance, (1) a maximum could be placed on the percentage of ownership in any corporation that can be held by any group of companies under the same or affiliated management, or (2) an individual director could be prevented from serving on all the boards of investment trusts which between them controlled more than a specified percentage of the stock of any corporation.

That is not against the law now. It is not in the bill, but it is entirely acceptable to us.

Opportunities for power and patronage. Entirely aside from the question of controlling other corporations, large aggregations of capital in the industrial field and elsewhere may have been criticized on the theory that their managements—if evilly disposed—are in a position, because of their size, to deal unfairly with labor or suppliers of materials. We point out that, in the case of open-end investment trusts, virtually no such opportunities for the abuse of the rights of others exist—regardless of the size of such trusts.

Organizations of this type do not buy large quantities of raw materials from suppliers, and hence cannot "grind prices down." Moreover, trusts are not large employers of labor. They buy nothing but securities, for which, like any other buyer, they must pay the quoted open-market prices. The only important business that they can award to others comes in connection with brokerage commissions on the securities they buy and sell; but even here, because such commission rates are standardized, there is no opportunity to "bear down" on those who render such services.

For all these reasons, we maintain that large aggregations of capital in the hands of open-end investment trusts are less likely to result

in the exercise of undue influence or power than in any other type of company. The managers of such trusts, although they may have large amounts of capital under their supervision, are so restricted by the very nature of the business and the rules under which they must operate that it is difficult to imagine any group that has less power to force its will on others.

In view of these facts, which are characteristic of most open-end funds, we submit that the criticisms that might be made regarding the concentration of a large amount of investment funds under a single management, under some circumstances, are not valid in this case.

Are there any questions, Senator?

Senator HUGHES (presiding). No; not now.

Mr. GRISWOLD. There is another matter in this bill that we should like to be recorded against, and which has not been discussed. That is the matter of voting rights of trust shareholders, under this bill.

This bill for Federal regulation of investment companies states that the interests of investors are adversely affected when investment companies issue securities containing inequitable provisions.

The language of the bill reads, "inequitable, discriminatory, or anomalous provisions, or failure to protect the preferences and privileges of their outstanding securities."

One of the purposes of the bill is stated to be the mitigation and elimination of such inequitable provisions.

In an effort to do this, the bill proposes that shareholders of open-end companies, including true trusts as well as corporations, shall be given the right to elect directors or trustees at annual meetings. In their application to true trusts, the proposed voting provisions are so sweeping as to require a complete departure from the basic principle under which such trusts operate. The basic idea of true trusts is continuity of management. A number of long-established investment trusts have been organized and built up on that principle. Their securities have been acquired by investors seeking continuity of management. In such true trusts, shareholders commonly have no voting rights. The trustees are permanent, subject only to removal by all or a majority of the other trustees, or by court action. In such trusts, many of the shareholders purchased their shares relying on the continuity of management.

It is argued that when investment company shares have no rights to elect directors or trustees annually, the result is inequitable because shareholders have no effective way of removing undesirable persons from control of such companies. The answer to this is that, in open-end trusts, the shareholders always have the right at any time to withdraw their capital at full liquidating value if they are not satisfied with the management. Moreover, the threat of such withdrawals because of bad management is the best incentive there possibly can be for good management.

The voting provisions suggested in the bill would outlaw most of those investment companies that are organized as strict trusts, and whose continuity of management is assured by vesting control in the trustees rather than in the beneficiaries. The voting provisions required in this bill constitute a death sentence for true trusts.

Trusts that are operated by investment counsel firms are typical examples of cases where investors want continuing management by a

particular group of individuals. Some of these trusts operated by investment counsel firms have been organized as true trusts in order to assure this. Another well-known type is the "common trust fund." These are operated by banks and are expressly exempt from this proposed act.

Investors in true trusts, in effect, choose their own trustees, at the time they buy their shares, just as an individual does when he appoints a trust company or chooses an investment counsel firm to manage his investments. The only difference is that, in the case of the open-end investment trust, the funds are commingled and the client's claim is represented by redeemable shares.

There are plenty of investment companies organized as corporations, with annual election of directors, in which an individual can invest if he prefers. There is no good reason why the type of investment trust in which shareholders do not have a vote to elect trustees should be outlawed. There is every reason why investors who prefer this type of trust, because it assures them the continuity of a specific management, should be allowed to choose it.

The type of investment company organized as a trust, rather than as a corporation, has had a long and honorable history in the management of real estate, especially in Massachusetts and in Illinois, as well as in management of securities. The oldest well-known investment trust of this character is the Boston Personal Property Trust, which has existed and prospered since 1893, or nearly 50 years. Purchasers of investment-trust shares are accustomed to this type of trust and have been willing to rely upon the integrity and judgment of trustees of recognized standing. In many cases the assurance of permanent management is definitely preferred to the plan of annual elections, whereby the management may be shifted from year to year. We question whether the Government's attitude should be so paternalistic as to deny the investor such a choice.

An individual who places his funds in a voluntary trust administered by a trust company can likewise terminate the trust if he is dissatisfied with the performance of the bank in question; but he is not entitled to force a change in the management or policies of the bank, which may be eminently satisfactory to most of the institution's other trust customers. Neither can a change in trusteeship be brought about by the beneficiaries of a common trust fund, which is a special kind of open-end investment company operated by banks and recognized under both Federal and State statutes. This same principle is also well established in the investment counsel field. In dictating by law, for the protection of investors against the people they employ to manage their investments, why differentiate between any of these examples?

Apropos of recent foreign difficulties, I might say, "Why should we be taken into protective custody," in respect to this and many other provisions of this bill.

If, however, the existing rights and protections are not deemed sufficient, we should have no great objection to giving the shareholders of true trusts——

Senator HUGHES. Do you call them "true trusts"?

Mr. GRISWOLD. I have been commenting on the S. E. C.'s plan.

Senator HUGHES. I say, do you call that a true trust?

Mr. GRISWOLD. Yes, sir; we are a true trust. We are exactly like a testamentary trust, except that our shareholders have certificates.

Senator HUGHES. I have often heard reference to the Massachusetts Trust as something that was created or devised by Secretary Olney.

Mr. MOTLEY. I think Secretary Olney very likely was the man. I think he was the man who drew the declaration of trust for the Boston Personal Property Trust, which is the oldest trust going.

I am not absolutely positive of that fact; but he was practicing at about that time, and I think I remember being told that he did draw the declaration of trust for the Boston Personal Property Trust. Incidentally, the Boston Personal Property Trust is exactly the same type of trust as these.

Senator HUGHES. Yes; that is right.

Mr. GRISWOLD. I was saying that if the existing rights and protections are not deemed sufficient, we should have no great objection to giving the shareholders of true trusts the affirmative right, by a proper majority, to remove trustees. There is a vital difference, however, between this "right of removal" and the provisions of the bill for "annual election" of trustees. If the right of removal is given, it seems to us that no complaint could any longer be made that the securities of such a true trust contained anything inequitable in this respect or failed to contain an equitable provision on the matter.

If such a right of removal by shareholders is to be given, it should, however, require the vote of a full majority of all outstanding shareholders, if not of two-thirds of all outstanding shares. The reason for saying this is, that in the case of any true trust, the whole idea of which is permanency of management, a change in management is a major matter vitally affecting the interests of those shareholders who bought into the trust in reliance on that kind of a management.

A change in management under such circumstances should not be lightly treated, as it would be, for example, if only the majority of a quorum were necessary—which would only be 26 percent if a bare majority attending a meeting. Matters that are major in the case of corporations, such as the sale of all of the company's assets, or a change in the general character of the business, or an increase or change in the capitalization, usually require the affirmative vote of a majority or of two-thirds of all of the outstanding shares, in order that the rights of minority shareholders, who went into the corporation on a certain basis, shall not be lightly overruled. Nor do we have any particular objection to a provision for annual or special meetings of the shareholders of true trusts, for purposes of allowing shareholders to vote on such matters as changes in the character of the business, or the removal or appointment of auditors, if this is considered wise. We do not consider it wise, ourselves; but it is a small point. At such meetings, the trustees could present the accounts of the trust, and shareholders should be given full opportunity to inquire into the management of the funds.

Mr. Motley has reminded me that I should explain one thing to you, Senator, which applies to these true trusts, of which there are a number in the business. There has been a lot of talk about "selling down the river." Where there is a management contract, the people who have owned the stock in the management corporation have sometimes "sold it down the river"; or where there has been an equity

stock, the people owning a majority sometimes have sold it to unscrupulous people—which is one of the evils we are all anixous to eliminate.

In these open-end true trusts, they are run by trustees. There commonly is no management contract, and there certainly is no equity they could sell; because the shareholders all over the country own that, and the trustees own only a very small percent.

It has been suggested that the trustees might sell out their office—in other words, that you could come to me and offer me so much money, and that I would resign, and the other trustees would elect, we shall say, Mr. DeRonde to take my place, and then another one of us would resign and we would elect some other man; and in that way we could sell out.

The answer to that is that it is absolutely impossible for us to do that; because under the common law respecting fiduciaries, if we were crooked enough to do it, the funds we would receive would themselves belong to the company, and we could not keep them; and if we did keep them, we would be guilty of an embezzlement. In other words, we cannot "sell down the river" if we want to—and we do not want to.

Does that answer that sufficiently?

Mr. MOTLEY. Yes; I think so.

Mr. GRISWOLD. Mr. Motley has also reminded me that I should state that there are several other true trusts, in the strict sense of the phrase, that are represented at these hearings and whose representatives intend to speak on this very point. I believe that the head of the Boston Personal Property Trust—which was Mr. Olney's trust—is here. They no doubt think that I go altogether too far in offering to compromise by giving the right of removal. They think that the people buy their trusts with the idea of absolute permanency in management; and I have no doubt that they will give you very good reasons why they think so.

We have one other short memorandum we can give you at this time, Senator, or not—as you please.

Senator HUGHES (presiding). Do just as you like about that, Mr. Griswold. My understanding with the Chairman is that we shall continue on until probably 20 minutes after 12, or something of the sort; and he may be back in the meantime.

I think he then will have to go to the floor of the Senate; I do not know what plans he has made for the afternoon.

Mr. GRISWOLD. Well, suppose I give you a rather short further statement.

The reason I say that is that the next speaker is going to have a very long speech to make, which would not be covered before half past 12.

Senator HUGHES. Then we had better take that in the afternoon.

Mr. GRISWOLD. Very well. Senator Hughes, I shall give you a short memorandum on one other matter. I am very sorry that your associates are not here to hear some of this, and I hope they will read it.

Senator HUGHES. Yes; I hope they will, too.

Mr. GRISWOLD. This memorandum has to do with bureaucratic censorship and red tape.

In the introduction to the Wagner-Lea bill, which proposes Federal regulation of investment companies, it is stated, as one of the reasons for the bill, that the national public interest and the interests of investors are adversely affected when investors do not receive adequate accurate, and explicit information, fairly presented, concerning offerings of securities.

There can be no quarrel with this point of view; but it has commonly been assumed that this was what the Securities Act of 1933 was for. The 1933 act requires that prospectuses be true to the smallest detail, contain all material facts, and be free from misleading statements. It also provides that it shall be against the law to transmit by mail any untrue statement in order to sell a security. It gives the S. E. C. the right to bring injunctions or refer such matters to the Attorney General for criminal proceedings.

Whatever other abuses there may be, one would think that the S. E. C. already had enough authority to protect the public against misleading statements and other frauds of that nature; but even though every investment company which offers its securities to the public is directly or through an underwriter already covered by the Securities Act of 1933, the Wagner-Lea bill proposes to subject the investment trust business to further bureaucratic censorship and endless red tape in connection with sales literature.

We are in entire sympathy with all sensible efforts to protect the interest of the holders of investment trust shares; but we do not think that end will be accomplished by snarling the entire business in complicated requirements involving registration, examination, reports, censorship, too iron-clad accounting methods, filing of literature and correspondence, and other complicated procedure. The type of thing proposed by the Wagner-Lee bill is bureaucracy for its own sake.

In this connection, Mr. Leon Trotsky, whose opportunities to watch the workings of bureaucracy have been almost unparalleled, recently said of what is going on today in Russia:

> The monstrous centralization of the entire industry and commerce from top to bottom, such as the compulsory collectivization of agriculture, was determined not by the needs of socialism but by the greed of the bureaucracy to have everything without exception in its hands.

Although the sale of investment trust shares is already regulated under the Securities Act, the proposed Wagner-Lea bill would make it unlawful for an investment company or its underwriter to employ in the sale of its shares any pamphlet, circular, form letter, or other literature unless it has been filed with the registration statement as an accompanying document, or as an amendment of such registration statement. Not satisfied with this, the bill then goes on to provide that every investment company, underwriter, and dealer shall make, keep, and preserve such accounts, records, memoranda, and correspondence as the Commission may prescribe, all of which shall be open to examination by the Commission. Thus will the S. E. C. undertake to tell everyone connected with the investment trust business just what correspondence and memoranda he must make and keep, so that there will be plenty of material available for any "fishing expeditions" that the S. E. C. may wish to conduct.

The chief objection to the filing of all literature and form letters with the S. E. C., except for the red tape and inconvenience involved, is that there can be no purpose in it unless the Commission establishes

a special department to censor every bit of literature issued by the industry; and if a censorship shall be established over all literature, not merely prospectuses, employed in selling investment trust shares, why not a censorship over all such literature put out in connection with the sale of all securities of every type in the United States?

Another objection to this filing of sales literature is that they say it must be filed as part of the registration statement. The result of that will be that even in an investment trust which has nothing to do with the selling and which is entirely segregated from the selling organization, each and every director of the investment trust itself will be liable for every misleading statement that may be made not by themselves but by the people who sell their shares.

It would mean that each director would be liable to punishment in the amount of 1 year in jail, if not 2, if the slightest mistake is made; because as underwriter, he is liable for every misstatement made, as I understand it, which is part of a registration statement.

This will mean endless delays. How can our selling house get out sales literature if they first have to refer it to us, as trustees, and then we have to refer it to our attorneys—and then, I might add, have it filed with the S. E. C.?

If the S. E. C. has to approve all the literature—and I suppose they do not want it unless they want to approve it—how long is that going to take?

Most of these investment-trust houses who sell the shares get out literature every week, in the way of weekly bulletins to all their dealers. There are thousands of dealers, all over the country, who receive articles not only about the investment trust, but about the course of the stock market and the effects of the war in Europe, and such matters as those. If this bill goes through, I suppose that will just have to be referred to us, and then we shall refer it to the lawyers; and that will be the end of that kind of thing. It will be utterly impossible, and it is utterly ridiculous.

Although the S. E. C. has no right to criticize such sales literature, from letters, and so forth, unless they violate the law, the arrangement would undoubtedly result in constant efforts by the S. E. C. to make changes in the texts of such documents, resulting not only in delay, but in outright censorship. No such requirements exist in the case of other types of securities, and it is difficult to see why the investment trust field has been singled out for such censorship.

Outlined below are some of the many ways in which the Wagner-Lea bill imposes bureaucratic authority and red tape on the investment trust business. Some of these provisions may be necessary to the administration of such an act, but many seem entirely unnecessary, while others represent useless duplication of procedure already required under existing laws.

I shall just state a few of these, to show you what we are going to be up against in this business:

First, all investment companies must qualify for one of the "classifications" specified in the bill.

Second, all investment companies must register with the S. E. C.

Third, all officers, directors, managers, investment advisers, underwriters, and distributors of investment companies must register individually with the Commission.