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HERALD TRIBUNE

230 West 41st Street
New York

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September 23, 1939

Judge Robert E. Healy, Commissioner
Securities & Exchange Commission
Washington, D. C.

Dear Judge Healy:

Following receipt of your letter of September 11th, in which you itemized various points in the article by Mr. Theodore Prince concerning the Maloney Act, I turned your letter over to Mr. Prince. Delay in replying has been due to the illness of Mr. Prince, but I have just received the enclosed letter from him in which he takes up in considerable detail the points mentioned by you.

Sincerely yours,

/s/ C. Norman Stabler

Financial Editor
NEW YORK HERALD TRIBUNE

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Theodore Prince
44 Wall Street
New York

Financial Consultant

September 22, 1939

Mr. C. Norman Stabler
New York Herald Tribune
230 West 41st Street
New York, New York

My dear Mr. Stabler:

I have received copies of the letter of Honorable Robert E. Healy, Commissioner of the Securities and Exchange Commission under date of August 17th, and September 11th, as well as yours of August 21st, to the Commissioner. Illness has unfortunately delayed my answering the communication in question of the 11th instant in which the Commissioner points out the bases of his criticism of my article appearing in the Herald Tribune of the 6th ultimo. He has been kind enough to express himself freely, and fairly, and I trust it shall not be amiss if I follow his example.

Under point one the Commissioner criticizes my failure to describe or mention the collaboration and approval of the various bodies he mentions, of the Maloney Act, and its passage by both "houses of Congress without a single dissenting vote". This did not seem material to me nor could I narrate all circumstances pertinent to those believing as well as disbelieving in the Bill. Unanimity of opinion does not necessarily indicate wisdom. The bases for its existence seemed far more important, namely its having become an integral part of the Securities Exchange Act of 1934. Particularly now in view of the Commissioner's point two that I failed "to indicate that the Maloney Act provides for voluntary registration of the associations of over-the-counter brokers and dealers.....". Now what is voluntary? And if the Commissioner's statement "that the Maloney Act provides for voluntary registration", be true what would happen if nobody registered? Since, therefore, I do not believe the registration is voluntary in a real sense, I could hardly be criticized, for failing to state it is voluntary.

Section 15, of the Securities Exchange Act of 1934 gives the SEC power to make rules and regulations for over-the-counter brokers and dealers providing for the regulation of transactions and for the registration of securities, and even for the registration of dealers and/or brokers. Accordingly this "pincer" process where something is going to be done if it is not done "voluntarily", does not quite seem to be a genuine voluntary process.

Under point three the Commissioner criticizes my statement about the SEC having the right to reverse any decision by the NASD but "also seemingly to 'run' the NASD....", etc. He selects three special instances, 15A(g), 15A(h)(2), and 15A(k)(2) which he feels does not justify my statement because under Section 15A(g) the SEC has "the right to reverse the decision of the NASD only insofar as disciplinary action against a member, or denial of admission to membership to any broker or dealer, is concerned". This seems to me quite a powerful check and control, and I do not find the SEC has that power against members of registered exchanges under Section 6. Under Section 15A(h)(2) the SEC, the Commissioner states, "may cancel, reduce or require the remission of any penalty; it has no power to augment the penalty". Again I feel this is sufficiently plenary power. Again the Commissioner states, the SEC "has no power whatsoever over the choice of officer or directors, except only as to the following: to satisfy itself that the method of choosing them is fair to all members; under Section 15A(k)(2) it can force the association to adopt rules concerning the method of choosing officers and directors;....the denial of membership or the disciplining of members; the method for the adoption of any change in or addition to the rules of the association; and affiliation between registered securities association. (*italics the writers'*)

The Commissioner closes this point by stating, "This power falls far short of the assertions made by Mr. Prince". I do not think so, from the Commissioner's own statement.

In point four the Commissioner states, "In paragraph seven and eight Mr. Prince quite overlooks the fact that findings of the Commission as to facts are conclusive only if found by a court, when challenged, to be supported by substantial evidence". I did not and I do not overlook that fact for I follow in my article by saying, "In every instance there is a hearing. But of what use is a hearing when a judgement can be sustained if there be evidence to support it? That means that an unjust or unfair decision always is based on some facts and evidence to support. It is another instance where men make the laws and construe them..." I do not mean that a commission can go haywire, but "substantial evidence" as the commissioner says, can in my opinion often support "an unfair and unjust decision", as I put it, and of that I complain and still maintain my post of criticism. Does not the Walter-Logan Bill aim to correct those very evils and allow of a more comprehensive review by a court, than is now afforded from the decision of a Commission? It does to judge from Representative Walter's claim that among other purposes, "It reforms a moot and arrogant system by which agency regulations are now issued and enforced". And observe what James M. Landis, regarding the White, Weld case, says in his book "The Administrative Process", "Though the finding of the Commission necessary to the issuance of a complaint is technically merely a finding that the Commission has reason to believe that the defendant has engaged in these activities, there is danger that the mental processes that lead to that conclusion may differ only by a matter

of emphasis from a judgement that the defendant has engaged in these practises".

I see no particular point in number five and I believe it has been already covered. Further the Commissioners own statement I believe justifies the excerpt, which he quotes, except that the SEC, so the commissioner states, "has no power to keep out of an association a broker or dealer who meets the membership requirements of the association". Would the association admit a member to whom the SEC specifically and substantially objected?

As to point six and seven if there be a soft impeachment of my reasoning detail or conclusion I do not feel it is sufficiently important or conclusive, to take up in detail unless the Commissioner would specifically request me to do so.

Point eight raised by the Commissioner is important for in it referring to sub-sections 15A(L)(1) and (2) he claims I have "garbled their meaning" by "failing to treat (1) and (2) as separate provisions". To garble has a vicious taint, and involves a sinister intent. Bismarck by garbling a telegram brought on the Franco-Prussian War. It is to be hoped that I shall not have caused more than the Commissioner's displeasure which I regret. In over twenty-five of writing I have never been charged with any lack of mental integrity because if I have been overzealous perhaps at times I have never been fired with any different zeal than that of the Commissioner himself with whose opinions if I may differ, I shall always respect.

My "garbling" is in reading the phrase "other activity" into paragraph (1) instead of leaving it in connection only with paragraph (2) where the Commissioner claims it belongs. As far as I am able to judge, the only difference is the penalty of revocation of registration of the association under (1) and expulsion under (2). Naturally I must condense in using newspaper space particularly in quoting statutes where I do no injustice to the sense and construction. I do not see why that should call forth the statement of the Commissioner that, therefore, (my conclusion which he quotes), "since it is based upon a careless and erroneous reading of the statute, can hardly be deemed sound".

I do not claim I am correct in my conclusion, but I do claim the commissioner has not proven me careless, garbling or erroneous. In quoting from the act an error appears in my article, paragraph 15, following the excerpts under discussion L(2) where the word willfully appears, which does not appear in the act; further quotation marks should appear after the word "under" four lines down, when the excerpt ends. A willful violation might offer some protection but evidently under this L(2)A a member may be expelled or suspended who "has violated any provision of this title or any rule or regulation thereunder, or has effected any

transaction for any other person who he had reason to believe was violating in respect of such transaction any provision of this title or any rule or regulation thereunder". This in effect I quote in my article and it is upon such omnibus and plenary embracing powers that I base my criticism. I do not feel the Commissioner has met my criticism. Is it possible he has placed emphasis of criticism on the form rather than the substance of my presentation?

Regarding the Commissioner's statement on page four as to my comments on Section 15(c) I should say I have no quarrel with that part of the Act which seeks to re-enact Section 10(b) of the Securities Exchange Act, now with those parts of the Act 15C(1) where "devices or contrivances as are manipulative, deceptive or otherwise fraudulent" are to be defined further by rules and regulations. Because there the nature and character of the acts are already defined by statute and the person is informed of the nature and scope of the prohibition, inasmuch as this is a Penal Statute. The Appellate Court accordingly then can more readily apply the law to the facts. That is the difficulty of the Section 9 A (2) of the Security Exchange Act of 1934 where intention rather than fact controls with a corresponding loss of certainty and understanding. Bureaus are thus encouraged to make decisions as men with varying individual judgments and conceptions rather than to interpret the law. That is what I meant to emphasize and did, not only under this point but under others raised by the Maloney Act of which I have mentioned in my article. I do not consider the references by the Commissioner on page four to the "power that the Trade Commission has had since 1914 to pass on what are unfair methods of competition" nor reference to the courts power "since 1892 to decide what are restraints of trade" at all pertinent.

Space does not allow for quote and re-quote and discussions that involve larger and more remote questions like the expanding circles of a still pool disturbed by a shower of disturbing objects.

The difference again is that unfair competition and restraint of trade has been objectively defined by Congress, and bureaus should administer, not legislate and thus re-define a whole course of punitive action. The line may be fine but it is the difference between administrative supervision and management between a democratic process and a totalitarian one. Fifty years of the I. C. C. well indicates the accumulative process of absorption of powers, that can give the right of a bureau to decide rates on a question of management and policy instead of only on a question of costs. Perhaps the point may be made clearer by an inquiry self-raised as to my accuracy in regard to this point raised 15C(1) and (2) last discussed by the Commissioner.

In my article (fourth paragraph up from the end) I approve the description and designation in C(1) but indicate such designation and description in the act was illusory because "the Act proceeds to give authority to the SEC who shall define such acts; which again places a broker and dealer at the mercy of such regulations as the SEC may lay down, to which regulations he must abide (if he can) whether they be clear or ambiguous, just or unjust". On careful reconsideration under this subsection C(1) and (2) can the SEC re-define and reform what according to their own individual judgment is meant by "devices or contrivances as are manipulative, deceptive or otherwise fraudulent" C(1) or will they "by rules and regulations define and prescribe means reasonable, designed to prevent, such acts and practises as are fraudulent, deceptive or manipulative and such quotations as are fictitious" C(2). If the former construction be correct my opinion set forth is warranted. If the latter construction be correct I believe I am in error in my final conclusion in that paragraph, of my article quoted above.

In that case my conclusion as to the construction pointed out was hasty, although as discussed, not yet settled.

You will observe I object to the whole cause of bureaucratic involvement of which this Maloney Act is another step forward. The Security Exchange Act of 1934 gives greater power to the SEC than the Securities Act of 1933 and in my opinion the Maloney Act gives greater power to the SEC than the Security Exchange Act of 1934 does. The fact that important, deliberative and intelligent bodies consent to the impairment of fundamental rights is merely an indication of the state of public opinion, or of the strength of the administration in power. It is a course of governmental procedure which I believe can lead to tragic results in the hands of men who fail in the high standards of integrity and conscientiousness now upheld by the present commissioners. There are points in my article the Commissioner has not touched upon perhaps the reverse may also be true. If there be any reflection on the SEC in my article they are unintentional and withdrawn. I have tried to confine myself to a rebuttal and do not mean to be controversial, but must sustain such honest opinion I have and express them frankly, which I have done.

Sincerely yours,

/s/ Theodore Prince

TP:MD

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON

ROBERT E. HEALY
COMMISSIONER

September 28, 1939

C O P Y

C. Norman Stabler, Esq.
Financial Editor
New York Herald Tribune
230 West 41st Street
New York City

Dear Mr. Stabler:

I wish to acknowledge and thank you for your letter of September 23, 1939, transmitting to me Mr. Theodore Prince's letter of September 22. I have read with care Mr. Prince's reply to my comments on his articles criticizing the Maloney Act and appreciate the frankness with which his views are expressed.

My disagreement with much of Mr. Prince's reply tempts me to a further detailed rebuttal. Since, however, the differences of opinion which exist between Mr. Prince and me already have been brought into fairly clear relief, I have decided to conserve your time and his, as well as my own, by avoiding the temptation. In closing this discussion, however, I should like to make one or two general observations.

In the first place, my purpose in writing you was not only to seek to correct what I conceive to be serious mistakes of legal analysis, but also to present some historical background essential to an understanding of the attitude of the members of the Securities and Exchange Commission toward the Maloney Act and their reasons for hoping to enlist the wholehearted support of the financial community in making this pioneering effort in the field of cooperation between business and government a success. Mr. Prince has addressed himself almost exclusively to the possibilities for maladministration which he reads into various sections of the bill and by implication to the horrors which might eventuate should an unwise or unworthy administrative body seek at some future date to exploit these real or fancied opportunities to injure the mechanism of our financial markets and through it the national economy. Mr. Prince does not deny the vast amount of benefit which can be derived by the financial community and the investing public if the roles delegated by the Maloney Act to this

Commission and to the brokers and dealers of the country are played with intelligence and understanding. In my correspondence with you I have undertaken to reflect the determination of this Commission that insofar as we are given the light our part will be so played. That by itself, of course, is not enough to insure the results we all earnestly desire. I, therefore, continue to hope that, notwithstanding such misgivings as may here and there be entertained with respect to fundamentals of the administrative process, this pioneering effort will be given a fair chance to succeed and that the brokers and dealers of the country will not be discouraged from carrying out their pledges of cooperation, without which the Maloney Act program cannot be a success and in fact would never have been undertaken.

Yours sincerely,

Robt. E. Healy,
Commissioner

P.S. "Garble" does not mean to me what it does to Mr. Prince.