

PARSLY BROS. & CO.

INCORPORATED  
1500 WALNUT STREET  
PHILADELPHIA

September 15th, 1933.

Mr. Baldwin B. Bane,  
C/o Federal Trade Commission,  
Washington, D.C.

Dear Sir:-

I am attaching to this letter articles appearing in the Philadelphia Public Ledger of September 13th, one having to do with a talk by Mr. Arthur R. Dean of Messrs. Sullivan & Cromwell, and one with your own talk before the Better Business Bureaus. These articles, each from men who are entirely serious and thoughtful in their expression, present contrary views. May I, as an interested party and at the same time with a considerable experience in the investment banking business intrude upon your time to express some views of my own.

I naturally and somewhat selfishly prefer that there be no Federal regulation of the security business. However, after the excesses and mistakes of the recent prosperity era, I recognize that some form of regulation was an inevitable result. The ideal that we should all strive for is some form of regulation that will protect the investor and not at the same time strangle the provision of capital for established industries or for those in process of being established.

To my mind there are two distinct fields, that of investment, and that of speculation. Each has its place. An investment banker should properly earmark as to the respective class the securities which he is selling and the investor should clearly understand just what he is buying. This condition has not always existed and to my mind is one of the serious past faults.

I think it is an indisputable fact that investors by and large are woefully ignorant; in fact, unbelievably so as far as any sound knowledge of securities is concerned. This applies as well to people of large means who have invested money for years as to people of small means and to too great an extent to commercial bankers. While there are a few exceptions investors in the main depend on someone for advice and are for the most part incapable of forming any opinion of their own as to the merits of a security on the basis of cold facts submitted to them. Running somewhat ahead of my story, I believe that a prospectus submitted on the basis of the Securities Act of 1933 will be beyond the comprehension of the vast majority of investors and I am satisfied that a very large percent of investors will not even attempt to read such prospectuses. I know from experience that it is hard to get them to read a circular of even the briefest character.

The investment banking business, as I see it, is a business in which it is practically impossible to have very definite rules or bases upon which to act. Personal opinions and judgments are basic and the skill with which such a business is conducted depends upon whether good or bad judgment is used. The lawyer and the doctor sell advice. The merchant sells commodities. The investment banker sells a commodity but he sells it with a mental attitude quite akin to that of the lawyer and physician. His commodity is expected to remain sound and productive in the face of an ever changing world. To be truly skillful he should see into the future and recognize what effect invention, discoveries, politics and economics will have upon the commodity sold. With this in mind any thoughtful person understands that the investment banker can never meet these conditions with complete accuracy. It is largely a question of experience, skill, foresight and judgment. To my mind any security regulating act should be based upon these hypotheses.

I have had to do with the Blue Sky Laws in a good many states. My personal opinion is that basically the Pennsylvania law is about the best. I do not mean that I regard it as perfect. I think it could be more rigid and some of the Commissioners have told me that they have endeavored to draw tighter lines but that their efforts to obtain essential legislation have always been thwarted. I believe that it would be a great step forward if we had an effective Federal Securities Act and if all State acts could be repealed. My view as to the best form for a Federal Securities Act is that it should establish a certain basis of integrity and ability for the people engaged in the business and then allow those legally able to engage in the business to operate with a fair degree of freedom. In other words, I think that there should be a Federal licensing board; that all partners and officials of investment firms should hold a license from this board, and that all employees other than purely clerical should also be licensed; that in order to obtain a license a certain experience and a certain knowledge of the business and of economics be required.

I quite appreciate that an objection to this is that in recent years some of the old and presumably experienced firms made quite as many mistakes as the less experienced. While this is true, I do not believe that it is a good answer. After our experiences of the past four years it is inconceivable to me how so many intelligent people made so many mistakes during 1929 and the period immediately preceding. When people now tell me that they knew that the economic ideas prevailing at that time were all wrong I know from personal experience that their statements are untrue. I do not know of a single person who definitely and clearly proclaimed in 1929 or earlier his distrust of conditions then prevailing. I know also from experience that the people who are today the most vociferous in their condemnation of bankers in general were the most rabid speculators in that extravagant period.

Our business was originally a conservative investment banking business. I was trained in that school and it is my natural inclination. In 1929 it was practically impossible for us to sell high grade bonds yielding a modest 5% or so. Conservative investors of former days would laugh at you. During that period everybody was buying securities not for income but for appreciation in market value. At one time we participated in an offering of the stock of an investment trust. It so happens that it was a fairly good trust and is still in existence. I almost created a riot by attaching to all of our sales a provision that a purchaser must hold the security

for at least 60 days. I did this deliberately to try to squeeze out people who were just buying for a quick turn.

These are rather aside from my principal thought but I introduce them to give some color of the conditions existing at that time. After four years of depression and trouble it is difficult for many people to recall their state of mind of a few years ago. One difficulty in the investment banking field to which I have seen no reference made and which I think was an unfavorable factor in the pre-depression days was the enormous influx of firms into the business. This condition as a matter of fact held over a long period of years. The increase in the number of investment banking and brokerage firms was out of all proportion to a normal increase in the volume of business. Any group who had the capital could engage in the business whether they were qualified or not and an undue number of young college graduates with good connections but with no experience whatever were sent out to sell securities. The advice of many firms and of their salesmen was necessarily of little value but the increase in the number of people in the business naturally built up over a period of years a highly competitive and very unsound condition. Overheads increased and then firms were forced to develop business in order to support the overheads; developing business meant that securities had to be manufactured and manufacturing securities meant unwise financing. There was great activity but it was thoroughly unsound and it was extremely pernicious in that it developed so gradually over a period of years that even those close to it did not recognize it.

My contention is that if during that time there had been in existence some restriction which would have held in check the number of people engaged in the business, those who were in it would have found, through perfectly legitimate channels, sufficient business to support them. If Federal regulation such as I suggest should come into existence I would be glad to have some real teeth in it to the extent of empowering the body originally granting the license to revoke the license granted on the ground that the performance of any given firm or individual was unsatisfactory. My opinion is that regulation along this line will in the long run be more satisfactory than the kind of regulation provided by the Securities Act of 1933.

Investment banking, from my viewpoint, should be a profession. Lawyers and physicians are required to undergo a course of training and to pass examinations. I should be glad to see the same situation apply to investment banking.

As between the views expressed by you and by Mr. Dean I must confess that I am inclined to favor Mr. Dean's position. I have read the Securities Act of 1933 numerous times. It always leaves me with a tremendous sense of vagueness. I know from my personal contact with investment firms of standing that they are unwilling to undertake financing because of the liability provisions. As far as my firm is concerned, we have every desire to conduct a high grade investment business and to observe the law but in many ways we are pretty much paralyzed. There are, as you know, thousands of investment securities. It is an impossibility for any firm to have more than a general knowledge of the great majority of issues. Avenues for obtaining information such as company reports, security manuals, etc. are open to us but there is always the possibility that there may be errors in these and if we unwittingly repeat the errors we

become liable. However, if left entirely free we could apply our own general knowledge and I believe interpret with a fair degree of accuracy. We formerly operated a Statistical Department which was, I think, efficient and which undertook to supply clients with investment suggestions and with information. This Department has practically ceased to function; we are afraid of the risk. We are not supplying clients with information except upon request. When information is supplied it is usually quoted from official reports or manuals; we designate the source of our information and hesitate to express our own opinion because we believe that if we did express an opinion we might be subjecting ourselves to liability in spite of the fact that we know that our judgment and opinion is superior to that of the average investor.

I do not mean to say that there should be no liability; I believe that we should be liable for failure to exercise reasonable care, for mistakes that could have been prevented through reasonable care, but there seems to me to be no reason for subjecting the investment banker to greater liability than is faced by any other business or profession.

In your address as I understand it, you took the position that lagging investments is the result of economic conditions and not of restrictions. In my judgment you are partially mistaken. I think economic conditions have had some effect but I believe the Securities Act of 1933 has had a greater effect. I have watched the list as published from time to time of the registration statements filed with the Federal Trade Commission and I must say that I think on the whole it is a rather poor exhibit. If the Securities Act of 1933 were amended as to certain of its provisions I am confident that within thirty days there would be numerous offerings of securities of good quality and which would really serve helpful purposes. Until radical changes are made in the Act I doubt very much if the most conservative firms will assume a constructive position in respect to new financing.

I must apologize for intruding to such great length upon the time of a busy man but this situation is naturally very much in my mind and I am taking the liberty of stating my thoughts to you.

Very truly yours,

E.G. Parsly

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