3

Betterment of Life Insurance Service

PROTECTING THE PUBLIC BY INFORMING THE INVESTOR

BY

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The human mind has lost its stabilizer. In its quest for another it is performing some curious side slips and nose dips. When the curtain dropped on the war we fondly hoped the next act would represent peace. Instead it has revealed a near approach to chaos. The stage is dark where we expected light. Speculation and waste are quarreling over who shall lead the orchestra. Amidst the Babel of noises the voices of the historian and the psychologist are silenced, and we, the audience, sit benumbed as we foolishly imagine this act a new one. If the historian could advance down stage and reach our ears, he would tell us that the sinister manager is plagiarizing an act as ancient as man. He would say that the fitful fever of speculation and waste invariably springs from the womb of war and runs its blighting career out to the end.

Recall your history as I quote a word picture and tell me who wrote this and what period it describes:

"Speculation ran riot. Every form of wastefulness and extravagance prevailed in town and country. . . . luxury of dress, luxury of equipage, luxury of table. Individual interests were again taking the precedence of general interests. . . . The spirit of gambling, . . . had swollen to its full proportions, and, in the garb of speculation, was undermining the foundations of society."

Or, again:

"The country swarms with speculators who are searching all places, from the stores of the wealthy to the recesses of indigence for opportunities of making lucrative bargains. Not a tavern can we enter, but we meet crowds of these people who wear their character in their countenances. . . . It is remarked by people very illiterate and circumscribed in their observation, that there is not now the same confidence between man and man which existed before the war. It is doubtless true; this distrust of individuals, a general corruption of manners, idleness, and all its train of fatal consequences, may be resolved into two causes—the sudden flood of money during the late war, and a constant fluctuation of the value of the currencies."

I have been reading from the historian, Green, and the Essays of Noah Webster on the American Revolution. Curiosity might lead us to many realistic descriptions of that period from other authors, but time bids us move on.

I pass the years following the War of 1812 with the mere mention that a like condition existed. The aftermath of the Civil War is so near to our time that you undoubtedly have heard of its feverish period of speculation.

Bullock, in his "Monetary History of the United States," says:

"Wages did not rise immediately in proportion to the increase of prices, so that the laboring classes suffered a considerable loss of their real incomes. Business was given an unhealthy, speculative impulse, which necessitated a severe period of liquidation in 1873."

Mitchell, in his "History of the Greenbacks," declares:

"It is therefore true that the monetary situation was largely responsible for the appearance of a considerable class of persons—of whom the fortunate speculator and the army contractor are typical—who plunged into the reckless, extravagant habits that called down upon their heads the condemnation of the popular moralist."

Greece, Rome, Napoleon, all saw the spirit of speculation, as distinguished from the spirit of production, following in the wake of wars. Yet with historic precedent pyramided upon precedent few of us really believed that we would follow the trail blazed in other periods.

We saw Europe forget how to laugh and learn to tremble. While we looked on the smiles faded from our countenances and righteous indignation hardened them. The silent voice of the psychologist would have translated this loss of laughter into terms of inflexibility, contraction, tautness of mind and muscle, and would have warned us that when the curtain fell on war there must come the reaction. We gazed on Europe gambling with life. Then we took a hand in the game and played with death either in reality or observed it in such a way that we lost the fear of its sting. Swiftly, but surely, we released the tether of conservatism. Not only the necessaries of life but even life itself lost its value. As the former began to be destroyed, the purchasing power of our currency started down the chute. Then the Hun quit. and we all broke training and relaxed. The reaction was so great that it not only unsprung our mental balance, but also our safety deposit boxes, from which have escaped many of our Liberty Bonds. This was the background and setting on the day when an emergency call came from the Secretary of the Treasury, the Capital Issues Committee and the Federal Reserve Board saying that there was such a speculative orgy in "wildcat" investments that the Victory Loan was in jeopardy. We were informed that in the neighborhood of five hundred million dollars a year were being absorbed in such investments, and that we were the only organization of the government that had jurisdiction to check this danger. We accorded these Departments a hearing, at which their legal representatives argued that under the Federal Trade Commission Act we had jurisdiction to order a get-rich-quick "Wallingford" to stop.

There were two questions to be resolved before we determined to set in motion the machinery of our Department. First, whether a security carried from one state to the other for the purpose of sale comes within the definition of an interstate commodity; and, second, whether the Liberty Bond, or any other legitimate security, competes in the financial market with a misrepresented "wildcat" stock for the possession of the investor's money. The Commission resolved both questions in the affirmative after thorough and deliberate study.

In the meanwhile the Treasury Department in its Victory Loan activities had requested those who were being asked to transfer their Liberty Bonds for what appeared to be, or actually were, stocks whose value was misrepresented to bring it to the attention of our Department. A searching questionnaire was swiftly prepared and in more than a thousand cases was sent to those against whom complaint had been made.

Of the hundreds of corporations that made reply forty answered that they had ceased selling stock immediately upon receipt of the questionnaire and would turn back the moneys on hand to the subscribers. Others continued until complaint was issued. A small group have joined issue with the Commission and are contesting its right to order them to stop. The issuance of the complaint does not convict the respondent. It simply indicates that after a searching preliminary investigation the Commission has reason to believe, and therefore under the statute issues a complaint.

Not until the Commission's witnesses have been cross-examined and the one complained against has put in his defense will the Commission say whether the respondent should cease the practice complained of. But "Wallingford" was quickly advised of the Commission's limitations. He is agile in his facility to meet opposition, and, like the coyote, he keeps just an irritating distance in advance. He soon learned that should the Commission issue an order for him to stop, he could prevent its immediate effectiveness by applying to the Circuit Court of Appeals for a review of the order.

What he feared most was the publicity of the Commission's complaint. This he circumvented by putting on a sales campaign with such rapidity as to make his clean-up and get away while the Commission's investigation was going on. Instead of a large capital stock he put on sale an issue, the par value of which was usually about a hundred thousand dollars; intensified and shortened his advertising campaign to a period of a week or ten days; spread his salesmen out over the territory, and reaped his harvest. Then he disappeared from that jurisdiction, but invariably reappeared in some distant state behind the barrage of a corporation with a name unrelated to that which had been the cause of his recent campaign.

Our questionnaire revealed a situation that we had not fully anticipated—the diversity of interests of those promoting stock sales. Despite the seriousness of the situation, the mere recital of the schemes devised to separate the people from their money presents a ludicrous statement. In order to advise ourselves properly we had to investigate each one of the schemes separately and compare the advertisements or representations with the value of the article. Consider a limited Governmental department investigating simultaneously many alleged inventions that are promised to produce a fortune; methods of catching fish; schemes for raising property lost at sea; hog raising; colonizing schemes for soldiers, and countless other devices. Remember that hundreds of companies are organized every year. Reflect on the rapidity with which the Department must function in order to be effective, and judge whether it be possible for any Governmental body to prevent misrepresentation in speculation.

You will note that I describe the evil by the word "misrepresentation." I do not believe in depriving an individual of his inalienable right to speculate. Speculative enterprises developed Cripple Creek, Goldfield, Leadville, and some of our greatest industrial successes. To limit speculation would destroy individual initiative. Should the government do this? Consider if it would have acted wisely had it done so in a recent notable instance of an oil company which was selling stock on a "shoestring." All that it owned was a prospect, a piece of land in unproven territory and machinery that was sinking a well. With undoubtedly much more surprise to the promoters than to the stockholders, that well in one day produced a thousand barrels of oil.

It is not speculation, but misrepresentation and the lack of information on the part of the prospective investor that must be eradicated. Let him know the truth and make his own decisions. The Master said: "Ye shall know the truth, and the truth shall make you free." He meant this truth to be personal. There are those who differ with this saying. They believe that the truth should be lodged in the minds of a few, and those few should be in the government service. They visualize that service in the symbol of a parental Uncle Sam, who says to his wards, "You can go into this investment because I think it is all right, but you cannot go into that because I don't think so."

As a Government official I would not want to have the power and responsibility of passing upon the issuance of a security in advance. Suppose one withheld his approval because of the speculative value. This might prevent the development of mining territory and oil fields which otherwise would become valuable National assets. Should he approve of an issue of securities, the public would read his approval as an endorsement by the Government. A subsequent failure of the security would bring condemnation and possibly retirement to private life. If the official were human, his future action on securities would incline toward the negative. Then the law would become inoperative. Moreover, with such a discretion and such a vast infinitude of information necessary, the careful official would want a department the cost of which would require a prohibitive appropriation.

In seeking a solution I have called upon my own experience. Some years ago I was adviser to the Insurance Commissioner of one of our states. That Commissioner had one remedy which he used effectively as a corrective—the specific which we in war times call propaganda; in peace, publicity. On an hour's notice he once called me into a case where certain agents were charged with misrepresenting to some farmers the terms of an insurance policy. The case was to be tried under a statute which had been recently passed and which forbade such misrepresentations by agents. Both of us had our doubts about the constitutionality of the act, but the arrests had been made, the prisoners were about to be tried and the district attorney had deserted us. When the jury retired and hours passed we began to doubt whether we wanted a conviction, fearing a reversal in the higher court on constitutional grounds and hence a destruction of a statute which because of its mere existence was a preventive to misrepresentation. The jury finally came in, after being out twenty-two hours, and freed the prisoner.

I was told by good authority this summer that the effect of the publicity of that trial was such as to eliminate the bogus insurance man to this day from that district. Conviction would not have materially helped in that case. Conviction rarely helps. Publicity is the effective remedy. From six years' experience in the Department of Justice and less than a year in the Federal Trade Commission I do not hesitate to affirm that the statute which, through publicity, seeks to prevent is far more efficacious than the one which is parental and punitive. Prophylactic law will prevent the wrongdoer where the punitive law will fail. When the human mind has broken down to the point where it wills to commit a crime, law will not stop it, but light will stay it. A criminal who would misrepresent or conceal can no more stand the light than could the darkness that filled this universe when the Master Architect, brooding over it, said, "Let there be light." It is because of the preventive remedy that I find comfort in the act which was drafted by Congressman Taylor in conjunction with the Capital Issues Committee, and known as H. R. 188. That bill makes the Secretary of the Treasury the repository of certain information which any person or corporation must file with him before it can put on an interstate sale of securities.

In so far as the bill gives him the power to make exceptions to this requirement, I cannot agree with it, and doubt whether any public official would welcome such power. The effective part of the bill lies in its placing the burden upon those selling the securities of telling what the assets are behind them, what sums are to be derived from their sale, the rate of commissions to be paid, and the availability of this information to the public.

The design of the bill is not new. It is drafted from one that has been a law for many years in a country far in advance of us in protecting its investing public. I refer to the law passed by the English Parliament in 1908, as amended.

When called upon to give my views to the Judiciary Committee of the House of Representatives regarding this bill, I was discussing the availability of the information which the government would require to be deposited with the Secretary of the Treasury, and also with the postmaster in each capital city of a state where the security in question was to be sold. I had reached that part of the bill where those offering the securities are required to insert in any advertisement of the same for sale a statement that information about the security could be had by writing to the Secretary of the Treasury, or the postmaster, when one of the members of the committee asked if such a notice would be entirely effective. This question struck at the one weak point in the British act which has made it far less successful than it might have been—the gap between the prospective purchaser and the official who has received the information about the security. This gap in the English law has been referred to by experts in finance. The Taylor bill attempts to bridge the chasm by requiring a statement in the advertisement that the data concerning the security could be had from the Secretary of the Treasury or the postal official.

To make the connection complete and to cast the burden thereafter upon the purchaser I suggested that the bill be amended so that whenever securities are offered for sale in interstate commerce all the literature or advertisements put out for the purpose of selling the stock contain the rate of commission or bonuses received for the promotion or sale, the names of the promoters and underwriters receiving them, and the net amount to be received by the original entity issuing the security.

Mr. Taylor's bill as amended will, I believe, go as far as human ingenuity and a public body should go in protecting the investor by informing him. Some form of legislation is certain to follow the present situation. The question is, Will it be in a preventive or paternalistic form?

Preventive legislation to be effective must relieve the official in charge of the responsibility of making exceptions. To make exceptions means to determine in advance. Placing in the hands of a public official the power to determine in advance will underwrite its failure. To discriminate between securities by making exceptions of some would place pitfalls in the way of this legislation on its journey through the courts that would surely defeat it.

The evidence is against those who say that the protection of the investor can be handled solely by the states through their police powers. Where the sale of the security is interstate the States may function, but then only partially. In at least sixteen of the States a violation of the "blue sky" law is only a misdemeanor. It is a very rare thing for one State to grant a requisition for the return of a person having committed a misdemeanor in another State. It is not to be understood that the work of the States along this line is in vain. Nor should Federal activity deprive or weaken the States in their efforts. A Department required by Congress to protect the investor should coöperate with the State officials in every way. Not only should there be coöperation with them, but the efforts of Federal and State officials should be supported by all citizens and organizations interested in seeing that that part of the unrest in this country due to doubt of and loss from investments be quieted by the restoration of confidence in them. This confidence can be brought about by a campaign protecting the citizen.

Were I starting a national publicity propaganda for informing the investor, I would disseminate a statement something like this:

"To the Prospective Purchaser:

(1) Beware of the glib salesman!

(2) Beware of the prospectus that promises much!

(3) Remember, the investment will keep. Don't hurry. Stop and study.

"When approached by salesmen, or through advertisement or prospectus, communicate at once with the 'Blue Sky' commissioner at your state capital, if there is such an official, and ask him what information he can give you.

"If you are an employee, consult your superintendent, or employer, or banker, or the nearest, most reliable business man. If a farmer, go to town and consult, preferably, your lawyer. His decision at the cost of a small fee may protect your entire savings.

"When approached by a stock salesman compel him to put in writing for you the rate of commission he is receiving—how much of your money goes to the company's treasury; how much will be used in developing the property or business, and that he acknowledges that you in buying are relying on his statements. If purchasing direct from the company, make it sign a similar statement.

"Finally, strike out all of the language of the prospectus except that which tells just what money the company has—what property it owns and where located—and what work it has done. Consider then your bank account and your debts. If you have a family, ponder over its needs; finally, make your decision upon the basis as to whether you can afford to lose the money, if the investment fails.

"If you learn subsequently the misrepresentation has been made to you and that you have been deceived and injured thereby, consult your nearest State or Federal prosecuting attorney."

The success of a government is measured by the contentment of its people. In the human soul the master instinct is the perpetuation of its kind. Man in the aggregate has the same instinct for perpetuation as the individual. This mass instinct, when in the perfect flower, is evidenced by what we call patriotism or love of country. That love is measured by the contentment of its citizens.

Gentlemen, let us resolve that we shall protect the savings of the investor by informing him. In this way we shall, as a nation, increase its contentment. We are on the eve, whether we wish it or not, of becoming a cloud by day and a pillar of fire by night to the distracted nations of the world. Let us make the people of other lands, when extending the helping hand to them, so struck by this contentment that they will understand when we say:

"I would not even ask my heart to say
If I could love another land as well
As thee, my country, had I felt the spell
Of Italy at birth, or learned to obey
The charm of France, or England's mighty sway.
I would not be so much an infidel
As once to dream, or fashion words to tell,
What land could hold my heart from thee away.

"For, like a law of nature in my blood,
I feel thy sweet and secret sovereignty,
And, woven through my soul thy vital sign,
My life is but a wave and thou the flood;
I am a leaf and thou the mother-tree;
Nor should I be at all, were I not thine."