

STOCK EXCHANGE PRACTICES

TUESDAY, JUNE 14, 1932

UNITED STATES SENATE,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committee met at 11.30 a. m., pursuant to call, in the hearing room of the Committee on Interstate Commerce, the Capitol, Senator Peter Norbeck presiding.

Present: Senators Norbeck (chairman), Brookhart, Goldsborough, Townsend, Walcott, Blaine, Carey, Watson, Couzens, Steiwer, Fletcher, Glass, Wagner, and Morrison.

The CHAIRMAN. The committee will come to order. Professor Ripley, of Harvard, is a witness now on the stock exchange investigation.

Senator COUZENS. Are you going to swear the witness?

The CHAIRMAN. Whatever you say.

Senator COUZENS. We have sworn all the other witnesses.

The CHAIRMAN. He is here at my suggestion in hopes that he could help us out a little. He has been before the Banking and Currency Committee before.

STATEMENT OF WILLIAM Z. RIPLEY, PROFESSOR OF ECONOMICS, HARVARD UNIVERSITY, CAMBRIDGE, MASS.

The CHAIRMAN. Doctor Ripley, you may proceed. Give your full name and address and occupation, and then proceed.

Mr. RIPLEY. William Z. Ripley, Harvard University.

Senator WATSON. What is your position there, Doctor Ripley?

Mr. RIPLEY. Professor of economics.

Senator WATSON. And how long have you been?

Mr. RIPLEY. Thirty-two years.

Senator WATSON. And were you connected with the railroads before that?

Mr. RIPLEY. No.

Senator WATSON. Never were in the railroad business?

Mr. RIPLEY. I was educated as a railroad engineer.

The CHAIRMAN. You are a railway director now, are you not, Doctor Ripley?

Mr. RIPLEY. Of the Rock Island, and I have been since the reorganization in 1917.

The CHAIRMAN. Proceed, please.

Mr. RIPLEY. We seem to be standing at a parting of the ways in some respects, due to the widespread phenomenon of separation of ownership of property from its management. It is getting to be an old theme now, but the events subsequent to 1929 seem to me

to indicate more and more clearly that the State must take hold. Among other causes for the protraction of this depression is the state of utter bewilderment on the part of the common people, not the wealthy people, not the farmers so much as those found from end to end of our communities, the industrial working class with a little money, the white collar workers up to those of somewhat more ample means. All of those people have been induced to entrust their savings to the care of others. There is nothing else to be done under city life and modern conditions but to turn over your property, whatever it is, except your house and your garden, for somebody else to manage. And this bewilderment at the present time, as I see it, arises from the fact that those who have assumed this duty have, in too many cases, been recreant to their trust. I might give many striking illustrations, but you know them as well as I.

Now, what comment I might offer to you would avoid, if possible, increasing this bewilderment. The facts are already pretty well known. We ought to have, perhaps, some more disclosure in order sufficiently to arouse public attention; but the real constructive thing to which I wish this committee might address itself is that of recommending legislation to meet this situation.

The public, a very large group, numbers millions of people. It has been estimated recently that stock holdings in the United States are not less than 18,000,000. I do not mean the number of people holding stocks, but stock holdings.

And the striking phenomena is—and this is particularly true in the public utility field, that the number of people who have taken a small flier—\$50, \$75, or \$100—runs into the hundreds of thousands. I might cite the striking case in the advertisements of Cities Service, for example, that over 1,000,000 people are registered security holders in a property which aggregates assets of over \$1,000,000,000. That is a modern phenomena. It makes even United States Steel, American Telephone & Telegraph, General Motors, and corporations of that size, seem of relatively minor importance as far as this great public interest is concerned.

Senator FLETCHER. Do you mean they are permanent investors or just speculators?

Mr. RIPLEY. Permanent investors. They have been asked, solicited even, particularly in the field of public utilities, to become owners. I have in mind Associated Gas & Electric Co., in which it is publicly advertised that not less than \$1,000,000 a week, in \$10 bonds—they were called baby bonds—are being sold at the present time: at the most difficult period industrially and financially, perhaps, for placing securities that we have ever known. To my thinking, the phenomena of the continuing thrift of people of this sort is very striking. The New York Times the other day in an article indicated that the postal savings banks—the public governmental accounts of the people in England were surpassing all previous records. Our postal savings have reached an all-time peak of \$700,000,000. If you gentlemen would visit an institution like the Bowery Savings Bank, the biggest savings bank in the world, and note the horde of people who come in there, filing in and out, to increase their deposits. This bank is now doubling its quarters. The common people do not know what to do with their money. I

suspect also that the savings banks do not know what to do with it, either.

What are you going to do about it? And I am glad of the opportunity to urge upon you that same suggestion previously made to this committee. Many of these abuses and evils which have been exposed at your public hearings—failure of the Bank of the United States; the Gillette Razor scandal; and the collapse of the Insull properties—all of these thrive upon secrecy. You would better stop short selling and speculation if everybody knew just what was going on among those companies than in any other way. Therefore, I urge once again that you exercise the Federal power as appurtenant to the taxing power, to require that all means by which the Federal income taxes are computed, should be disclosed upon standardized, accepted forms prescribed by the United States Government.

Senator COUZENS. How frequently would you have that done, professor?

Mr. RIPLEY. I think that has got to be determined by experience. The result of a little book which I published a few years ago, called Main Street and Wall Street, has been, in five or six big corporations, as they have written me themselves, to demonstrate the feasibility of quarterly statements. Some of them had never reported before oftener than once a year.

The most pitiable thing about these great collapses is the lack of information among the owners. I am not urging upon you that the widow and the orphan can analyze corporate accounts. But there are professional analysts by the hundreds who get their living that way. There are research departments through which this information would soon be made available, thus becoming public property.

Senator BROOKHART. They are found too often on the pay rolls of those fellows, employed to boost stocks and bonds.

Mr. RIPLEY. That is true. But now it is all a guess. Nobody knows. A few corporations have adopted a fairly sound policy in that respect. The United States Steel Corporation deserves a good deal of credit. From the first day it published, in a full page of the newspapers, the complete condition of their company.

Senator COUZENS. Is it your opinion that that would have any effect on the bull and bear pools?

Mr. RIPLEY. I think so. When a man tries to run a bull or a bear pool he does it because of the lack of information, among the public, largely. If there were a Federal bureau which, as for the railroads, compiled and issued this material, you would have a check upon such affairs. It is, of course, a difficult matter. The New York Stock Exchange has tried to do it for a number of years; but they can not accomplish more than a certain amount. In the first place, they can only deal with those companies which voluntarily put their heads in the noose, through listing on the exchange.

Senator BROOKHART. Now in regard to the railroad stocks, in spite of the Interstate Commerce Commission, has there not been about as much speculation in the railroad stocks?

Mr. RIPLEY. Not so.

Senator COUZENS. No; I think there has not.

Senator BROOKHART. There has been plenty of it.

Senator COUZENS. There has been no bulling of the market.

Mr. RIPLEY. Railroad securities have just gone down, as they had to do under the circumstances. There has been no wild fluctuation as there was a generation ago. Where will you see anything like this Auburn business?

Senator COUZENS. It is outrageous.

Mr. RIPLEY. It is outrageous. I should like to show you letters that come in to me from the common people, school-teachers and white-collar workers. They have been done out of the product of their thrift and industry. It is not always by fraud. Corrupt practice is not always evident. Not infrequently when the business is going on its way, honestly and decently conducted, but without making full disclosure of the state of its affairs, these dealers in New York who have no other interest besides speculation as a living, will, nevertheless, play with it one way or the other by manufacturing information through means disclosed through this committee.

Senator FLETCHER. Would you have those statements apply to every concern listed on the stock exchange?

Mr. RIPLEY. I would go farther than that, sir, and require that any business engaged in interstate commerce, with more than a certain minimum number of stockholders, with assets of more than a certain amount, and so forth, should be required to make, either to a bureau of the United States Treasury Department, because they handle the income tax, or to some other bureau such statements. Those statements ought to include those things now currently reported. They ought also to include particularly such matters as depreciation, which is just a football in the hands of the unscrupulous in corporate accounts. The matter of the form of statement would have to be carefully provided for by cooperation between good representative business accounting organizations and the Government. It has been done for banks for years, although it is not even yet done properly. Bank accounts ought to be more intelligible and considerably amplified.

Senator BROOKHART. Do not bank stocks vary about as much as any stocks?

Mr. RIPLEY. If so, that may be due to the imperfection of those accounts as now rendered. But with the railroads, publicity of their affairs, has among other things put the railroad out of politics. They are not in politics now, as they used to be 20 years ago, when I first knew the business. Publicity has been also extended to telephones and telegraphs. There is no reason in the world—and I have asked the advice of good constitutional lawyers—there seems to be no reason in the world why this same requirement might not be extended to industrial corporations which are of a sufficient size and public importance to warrant the procedure.

Senator FLETCHER. Doing an interstate business.

Mr. RIPLEY. Doing an interstate business, of course. You could not take hold otherwise.

Senator GLASS. I think I asked you when you were before the committee before, more than a year ago, this question: Do you think it is impossible to define the difference between an investment and a pure gamble in securities?

Mr. RIPLEY. I will tell you frankly how I feel about this speculative and gambling end of it. A good deal as I do about gang war-

fare. I would let them shoot each other up until they are all alike cleaned out.

Senator GLASS. The trouble is that they shoot everybody else up.

Mr. RIPLEY. That is true, but if there were disclosure currently of these corporate affairs, it would at least be a damper on such activities.

Senator GLASS. But, Doctor, the average man, who is not an expert, does not understand these matters. Do you think a man invests his money for an hour, or a day, or a week, or a month? Do you call that an investment?

Mr. RIPLEY. No more than I would a man who takes a flyer in the Irish hospital sweepstakes. Hundreds of people do that. But there are also people of another sort. These have impressed this on my mind, because I get so many letters, which run like this: "I am a school-teacher. I have invested three years' earnings in Schulte Retail Stores. Nobody on earth knows less about Schulte Retail Stores than I do, and I lost my money. Yet nobody can tell me how or why it has all come about."

Senator GLASS. To come back to my question, do you think it is impossible to define the difference between an investment and gambling?

Mr. RIPLEY. It is as indefinite a line as the difference between right and wrong.

Senator GLASS. Well, I think I called your attention to the fact, more than a year ago, that I had prepared a chart which showed that the average period that stocks which passed on the stock exchange, six or seven years before, was held 30 days, and that had been reduced to 22 days. Do you think people invest their money for 22 days.

Mr. RIPLEY. Now, Senator, I would, right at the start, strike down the validity of those figures, for this reason: Speculators are selling a hundred times over, while those other people invest but once. When you arrive at that figure of 22 days, you are including an overweight speculative transaction on the stock exchange. The people I have in mind are those who are buying utility bonds at the rate of \$1,000,000 a week. There is no market for those bonds. There is no way to dispose of them. Those who take them take them for keeps. They can not speculate if they would.

The CHAIRMAN. What is the name of the concern, if you do not mind telling, Professor?

Mr. RIPLEY. I am perfectly willing to say. It is the Associated Gas & Electric Co.

The CHAIRMAN. Is that the one about which there was some criticism or remarks in the papers because of refusals to put an address on the air?

Mr. RIPLEY. This same issue of the small investor I was asked to discuss before the National Association of Savings Banks. After the arrangement for the address had been made an offer was extended to broadcast it. I gave the text of the address to those in charge. They said it was not the policy of the National Broadcasting Co. to name names. I said I had been naming names all my life. You either take the broadcast as I read it, or you do not have it all. And so it was delivered but was not broadcast at all.

Senator GLASS. Doctor, what I am trying to arrive at—and I do not want you to get away from the point—what I am trying to arrive at is some accepted definition of an investment which could be taxed by taxing transfers of stock on the New York Stock Exchange, which did not conform to that definition.

Mr. RIPLEY. The dividing line is so indefinite that it is very difficult to draw up such a definition. I would say in this pending crash of Kreuger & Toll, a quarter of a billion dollars of securities have been sold to the American people.

The CHAIRMAN. What amount did you say?

Mr. RIPLEY. A quarter of a billion.

The CHAIRMAN. \$250,000,000?

Mr. RIPLEY. Yes, sir.

The CHAIRMAN. You have reference to stocks, or bonds?

Mr. RIPLEY. Both, all along the line.

Senator GLASS. They were sold as an investment.

Mr. RIPLEY. Yes; they were bought and sold—

Senator GLASS (interposing). I am talking about those securities that are passing on the exchange, and you must stand by and find out what they are offered for to-day, and the day they are offered.

Mr. RIPLEY. One can sometimes differentiate, by experience, those corporations which are essentially speculative from those which are not. Such corporations pass from one state over to the other. I can take you back a few years, citing American Can. It was highly speculative. Everybody was playing with it.

Senator GLASS. Those are the people I want to get out. Not those who buy for an investment, but those I want to get out, the ones I am talking about are those who gamble on American Can, buying it to-day, and gamble on what it will be like to-morrow.

Mr. RIPLEY. I would go along with you in any practicable attempt to minimize all such dealings.

Senator GLASS. That is what we ought to do.

Mr. RIPLEY. But my opinion is, Senator, you would discourage speculation more effectively by insisting upon a state of affairs where all of those companies shall have nothing to play with. If, once a quarter, the real status of Auburn Motors was made known; if Radio-Keith-Orpheum, and those other companies, that were up before you, were not blind pools, you would find that speculation would have quite a lot of the heart taken out of it.

Senator GLASS. That would affect the professional traders. I asked Mr. Mitchell, when he was before this committee not long ago, if 10 per cent of the people who take fliers, as your expression is, in market transactions had any knowledge whatsoever of the earning power or the management of the companies who were issuing those various stocks, and he said he did not think 10 per cent had.

Mr. RIPLEY. American Telephone & Telegraph has become a national corporation. The men who represent it on the board of directors are not there because they have a proportionate investment; there are men on there, like Daniel Willard, I suppose, who was put on because he was personally a national asset. The affairs of the American Telephone & Telegraph Co. are public property under the provisions of law which require that their earnings shall be filed, as railroad earnings are filed, with the Interstate Com-

merce Commission. You do not find Western Union played with to-day as in the day when Jay Gould had it in hand. Why? Because Western Union has to disclose its assets, and whatever is going on.

Senator COUZENS. That is true of A. T. & T.

Mr. RIPLEY. Exactly the same way. It seems to me, as a practical measure, Senator, directed to the same goal which you have in mind, that this would be most effective. There is grave difficulty in defining the difference between a speculator and an investor. The whole thing is a product of the war. It was these great salesmanship campaigns in Liberty bonds which taught the consumer of electricity, and the farm family—if the farm family ever has any money at all these days—to take the money out from behind the chimney piece and to buy one or two or three shares of the local utility. And, by the way, the workingmen, the employees of some of these corporations and utilities, have been too often forced to make the investment. That is one of the things that is going to come out in this Insull situation in Chicago.

The CHAIRMAN. In other words, we will find that the men were forced to buy their securities or lose their jobs?

Mr. RIPLEY. I have many letters saying that I was obliged to buy or I would have lost my job if I had not bought this—we commonly call it stuff.

Senator COUZENS. But the aggregate of that is not very great.

Mr. RIPLEY. I did not mean to say that it is the basis of it. And please do not understand me to say that I decry this investment in public utilities. It is a great growing industry which, in the main, is soundly handled.

Senator BROOKHART. Do you value speculation; has it any legitimate value in business?

Mr. RIPLEY. Not very much.

Senator BROOKHART. Then why not set an arbitrary definition between speculation and investment?

Mr. RIPLEY. If we could.

Senator BROOKHART. We could all right.

Senator GLASS. We could propose it, but I do not think we could get it through.

Senator BROOKHART. And would it not be better for business to live under some of the inconveniences rather than go on with speculation?

Mr. RIPLEY. Would it deal with the business effectively? Would it not hamper the man on the border line?

Senator BROOKHART. Suppose it does. Could he not afford to submit to that rather than have speculation?

Senator GLASS. I think those hundreds of thousands of people who bought A. T. & T. in response to a perfectly legitimate financing campaign were investors.

Mr. RIPLEY. Those people did not buy through the company.

Senator WALCOTT. They did not sell their own stock?

Senator GLASS. A. T. & T. did. They conducted an elaborate campaign of salesmanship. The stock was offered to me over and over again.

Senator WALCOTT. I think that is true.

Senator GLASS. And being a man of average sense I did not buy it. And talk about the matter of a statement of their condition, I will

tell you I do not think half of the Senators and Representatives in Congress could understand it.

Senator COUZENS. If that is true, why is this bulling and bearing not done with railroad stocks?

Senator GLASS. It is not variable, that is all.

Senator COUZENS. It is because they have to report to the Government. And for years they have done it.

Senator GLASS. We have not a man in this room that can tell me what is the condition of the Pennsylvania Railroad. You can not.

Senator COUZENS. Yes; I can.

Senator WAGNER. Would you not try to find out if you intended to invest in them?

Senator GLASS. No; not if I wanted to speculate. I would try to find out what it would be to-morrow. And they transfer ten times as much stock, frequently, in one day as the institution has put out.

Senator WAGNER. That is not true of rails.

Mr. RIPLEY. I do not see how you can define the border line between the two.

Senator GLASS. I can define it mighty quick if they would let me do it; and I would put enough money into the hands of the United States Treasury to repeal these measures of high taxation, or break this gambling up.

Mr. RIPLEY. Suppose I bought Gillette Safety Razor and to-morrow found out the real facts and sold it?

Senator GLASS. That would be an exception. One-tenth of 1 per cent. That would be an exceptional case. That would not be touched by the plain definition of the distinction between investing and gambling.

Senator WAGNER. It is difficult to make that distinction.

Senator GLASS. I do not think it is. It is suggested that it might be inconvenient. It might have been inconvenient to you in the Gillette Safety Razor business, but the immense good accomplished in other directions would override that.

Mr. RIPLEY. Of course, Senator Glass, you would have great trouble with fictitious accounts. You have already in your records before this committee had ample demonstration of fictitious accounts. I just wonder if it would be workable, however desirable the end might be. And I am aiming at that same end you are.

Senator GLASS. The stock gamblers thought it would be workable. When I proposed it in the Senate they got busy.

Senator WAGNER. Doctor, I wanted to ask you if in addition to this information that the public ought to have—and I think it is one of the greatest preventatives—would it not be well for the Government as well to supplement that information as well to the general condition of the country; such as a tabulation of the unemployment situation?

Senator WALCOTT. The Department of Commerce is doing that.

Senator WAGNER. We have not yet devised a proper system to do that, although we passed some legislation some time ago that passed under my name. That is difficult to do.

Mr. RIPLEY. At Harvard for quite a few years we attempted to do that. I never had anything to do with the Harvard Economic Service, but three or four of my colleagues did, and if ever there was a disinterested service, it was that. It was an honest endeavor

to give a true picture. But it proved difficult and unworkable. It seems to me, desirable as that information might be, too many people would come back at you, if they acted upon any advice that you gave, that I would rather make a beginning along this line of a simple statement of facts. And may I say—

Senator WAGNER (interposing). I did not intend it to take the place of your suggestion but that my amendment would supplement it.

Mr. RIPLEY. I would like to think it over.

This question of publicity is up all along the line. And with your permission I would like to file an editorial from the Journal of Commerce, of May 23, 1932, upon this plea which I made to the Savings Bank Association.

The CHAIRMAN. If there is no objection, it will be printed in the record.

(The editorial is printed in the record in full, as follows:)

ADVICE TO SMALL INVESTORS

Enormous losses have been suffered by thousands of men of small means who, in years of prosperity, invested in securities of a speculative type not suited to their special requirements. Many of these unfortunate people now realize the folly of placing savings that may be needed in emergencies in stocks and bonds of fluctuating and uncertain values. The passion for speculation and the lure of risk taking are irrepressible and will always claim a large number of victims who can not be protected against themselves.

There is, however, another class of small investors who, having no wish to gamble with their hard-earned savings, nevertheless fall a prey to ignorance of the speculative character of the enterprises in which they are induced to place their money. To investors of this type, who want safety but fall through lack of knowledge to obtain it, the address delivered by Prof. W. Z. Ripley of Harvard before members of the National Association of Mutual Savings Banks, carries a special message. His plea for open, sound, and intelligible standardization of the accounts of public utility companies, with Federal regulation of accounting practices as a safeguard, is also of particular concern to the managers of institutional investment agencies, such as the mutual savings banks, which hold in trust funds deposited by millions of small investors.

The recent collapse of two great holding company systems, one in the United States and one in Sweden, has afforded startling evidences of the dense ignorance of supposed experts and financial advisors regarding the involved accounting practices and mispractices of organizations whose bonds and debentures have been widely recommended as sound investments to the people of this country. These revelations emphasize the need for full and authentic information to throw light in dark corners, where dishonest manipulators work, and to give facts about concealed operations which, even when legitimate, ought to be known to prospective investors.

A great many people are inclined to waste time bemoaning the losses of the past, but doing nothing to protect the investors of the future against the same kind of exploitation to which they themselves have been subjected. Professor Ripley is doing the public a great service, therefore, in emphasizing the need for speedy action and the value of a positive program. In forceful language and with the aid of profuse illustrative material distressingly specific in character, which prevented the broadcasting of his remarks, he called the attention of savings bankers to the need for reforms in public utility accounting practice. He urges full and enforced publicity not only as a means of accordng increased protection to investors but also to the industry itself, since its growth and sound expansion are dependent upon utilization of the savings of the American people.

As Professor Ripley said: "A major development of public-utility finance is the far-reaching campaign to bring about customer ownership of such securities. The immediate future is big with possibilities of such a rush of popular investment. The public-utility industry, quite deservedly when properly managed, has been more nearly depression-proof than any other branch of investment."

Unfortunately, the solid character of the industry does not protect from loss the investor who acquires interest in mismanaged paper companies many times removed from the operating organizations that are depression-proof. It does not prevent him from sharing in speculative ventures, if he invests in bonds of public-utility companies whose underlying holdings may be of a speculative character. Professor Ripley is asking, therefore, that the investor shall be placed in a position to know what he is doing when he invests in public-utility issues. He believes that the investor ought to be told when a bond is not a senior obligation but merely a junior claim upon the unstable earnings of many scattered companies, of varying degrees of soundness. The present complexity of organization, moreover, frequently confuses the expert as well as the man of average intelligence and facilitates manipulations that defeat the purpose of regulatory safeguards.

Although the demand for full publicity, greater simplicity, and uniform practice in public-utility accounting is advocated by Professor Ripley primarily in the interest of the investor, it is plain that uniform, comprehensible accounting acts also as a check upon the efficiency of management. Hence, it assists the work of the regulatory bodies that are chiefly concerned to protect the consumer against excessive charges. Professor Ripley's words no doubt have aroused a timely interest in an important subject among representatives of institutions that control over a third of the savings deposits of the country. It is a pity that he was unable to reach the large audience of small savers, who stand in need of instruction and protection.

Senator BROOKHART. Mr. Chairman, I would like to ask another question or two about the stability of railroad investments. I am in full accord with your publicity idea, but is it not true that the publicity as to the earnings of railroads by law tended to stop speculation, more than the publicity?

Mr. RIPLEY. I am not aware of any considerable speculation since, at least, the Federal or War Administration. There is not a road one can play with, because the moment anybody tries to organize a pool somebody else gets in touch with the Interstate Commerce Commission and says: "Are their earnings really falling off or are they holding up?" The minute you get that public—

Senator BROOKHART (interposing). That is not my question. My question was, do not the earnings put on the railroads by the law tend to stop that speculation, and that complaints made to the commission are on the basis of the limitations of the law; that is, for instance, 5 $\frac{3}{4}$ per cent, and a recapture of half over 6 per cent?

Mr. RIPLEY. As things have gone in the last few years, it is not limitation on the earnings by the Government; it is the limitation put on the earnings by competition on the highways and the waterways and other ways.

Senator BROOKHART. But there is an excess of earnings of millions of dollars now.

Mr. RIPLEY. Yes; by a very few companies, such as the Chesapeake & Ohio, and the Norfolk & Western.

Senator COUZENS. May I point out that it is not only outside competition; it is inside competition that has helped, favoritism to shippers, and multiplicity of building warehouses, and so on, has contributed a large part.

Mr. RIPLEY. Yes; that is so. And while earnings have slid somewhat before, the toboggan slide has had a more or less steady grade. The line goes like this [illustrating], following what you might call the trend, due to fundamental circumstances, all the way up or down.

Senator BROOKHART. There isn't anything to play with in co-operative markets.

Mr. RIPLEY. Is there an open market? You have to have an open market before you can have speculation.

Senator BROOKHART. They do not need it. Now the English co-operatives are about the best institutions in Great Britain, and they have an absolute fixed arbitrary earning for their capital, do they not?

Mr. RIPLEY. Yes; I suppose they do. I do not know.

Senator BROOKHART. Well, they do all right, and that stabilizes them and destroys speculation entirely in their enterprises, and their percentage of gross is considerably greater than the gross of private business, and has been ever since the war. And its stability is assured, and it is stabler and sounder than anything else. So why can not we prescribe some way of limiting capital earning and stop this speculation? Of course, the definition suggested by Senator Glass would do that.

Mr. RIPLEY. I am not objecting to his remedy, but I am asking you how you would deal with the man who buys and has got to sell the next day because he needs the money for something else? It may be an emergency with him.

Senator GLASS. Are they not very few, contrasted with the great body of speculators?

Senator BROOKHART. I could write a definition in the law which would distinguish between an investor and a speculator and give the investor the benefit of legitimate investment of his capital, and if he could show a fraud was practiced on him he would have certain remedies against those who sold him the stocks or bonds.

Mr. RIPLEY. That would make difficult work for the courts.

Senator BROOKHART. It would not make anything like the increase in losses we have now.

Mr. RIPLEY. What you say may be true, but I would like to see this simple, practical remedy of corporate publicity applied first.

Senator FLETCHER. Doctor, let me ask you a question: The reason why we do not have this speculation in railroad stocks is because we have some governmental supervision over the railroads. Now, applying that to the stock exchange, there is the greatest financial institution in the world, the New York Stock Exchange, without any regulatory power or supervisory powers anywhere. Now suppose we undertake to regulate that institution by the Government, would not that be helpful in this matter of preventing these collapses, such as happened in October of 1929, and in 1930?

Mr. RIPLEY. That raises an entirely different issue, as to what was the cause of the collapse in 1929.

Senator FLETCHER. Well, to get back to this thing we have in mind, that is, the Stock Exchange, whether there isn't a regulatory power required on that?

Mr. RIPLEY. I will answer that, then, directly. I think that independent standardized publicity would do more than you could hope to do in any other way. Because, can you not see, sir, that the stock exchange can only deal with those who list upon it? I am urging that all companies, whether they list or not, should be required to make periodical statements.

Senator TOWNSEND. Doctor, would you go farther than banks are required to go at the present time?

Mr. RIPLEY. I do not know enough about bank accounts to answer specifically; but I have a very definite impression that it was the weakness of its requirements which rendered possible some of the bank collapses we have had.

Senator TOWNSEND. I presume you have noticed that the decline in prices of bank stocks has been quite as severe as in any other line.

Mr. RIPLEY. I would expect it to be more so, because the banks lie just a little nearer to the causes of collapse.

The CHAIRMAN. Doctor Ripley, may I ask your view on another matter? Is not a part of the trouble that people who hold positions of trust in these corporations betray them? Would it help if there were a restriction on officers and people selling stock under fictitious names while they are in charge of the property?

Mr. RIPLEY. I would like to see this committee recommend a measure, alongside of the requirement of reasonable publicity for all corporations engaged in interstate commerce above a certain size, something which shall deal with speculation by directors of great corporations in the stock of his own company. The officer in one of these companies is unlike the ordinary shareholder, because, while he continues to manage, he can step in and out of ownership with the greatest ease. I happen to know of some cases in detail of the administrators of great businesses who had a heavy investment up to 1929, which they completely unloaded at the present time, large companies that have even gone into receivership, but by reason of advance information the directors stepped out from under. The only way to deal with that question would be publicity. I would like to see some requirement that periodically the president and the members of the boards of directors of corporations, sufficiently imbued with a public interest, should make a showing of the number of shares which they hold. And I would add very severe penalties for evasion through the use of fictitious names. One of the best safeguards for the great body of people who are looking around for a safe placement of their savings, is that the men who manage that business are staying with it; that the captain is still on the ship; that he has not taken to the lifeboat, steering it by radio.

The CHAIRMAN. And telling others to stay in.

Mr. RIPLEY. Yes; and sending out wireless messages for others to stay or even to come on board.

Senator TOWNSEND. That the ship is safe?

Mr. RIPLEY. Yes. What happened in Gillette Razor and Kreuger & Toll? There was undue credulity. None of the steps were taken that they should have taken, to have audits made; to have their lawyers examine the concessions, to be sure they had actually been made and that nothing could go wrong. The whole Kreuger & Toll business was for the creation of a monopoly on a prime necessity of life, matches; that is to say, fire. In other words, a tax on matches is like a tax on salt. Those who get the exclusive right to sell salt or matches through selling third-rate Government bonds are resorting to bribery for a license to extort.

Senator WALCOTT. That is, by the Government?

Mr. RIPLEY. They got a Government monopoly on a necessity of life. The whole theory of the thing from the start was false. But I do not believe there was any corrupt purpose on the part of those

who placed those securities in America. I know some of those men. They were of marked integrity, but of incredible stupidity.

The CHAIRMAN. They did not look into it?

Mr. RIPLEY. They put their own money into it.

Senator WALCOTT. What about Ernst & Ernst?

Mr. RIPLEY. Did Ernst & Ernst go to Sweden? Did they do anything but take the figures presented to them by Kreuger? That is the trouble with a great deal of the auditing that goes on now. The auditor is looking at two sets of figures to see—

Senator WALCOTT (interposing). If it is in balance, that is all that is required?

Mr. RIPLEY. That is too true. And you will find there is often in the certification a little notice that reads something like this: "Having examined the figures submitted to us, this audit is correct," or "to the best of our knowledge and belief."

Senator WALCOTT. They may not have looked into it carefully.

Mr. RIPLEY. Yes; they do not say we have gone to the bottom of this whole business and pledge our reputation that all is exactly as it is set forth.

Coming back to your question, Mr. Chairman.

The CHAIRMAN. I do not remember what that was, but I am going to ask you another one. You said \$1,000,000 of baby bonds were being sold to small investors at the present time.

Mr. RIPLEY. A million dollars worth a week.

Senator WALCOTT. Of one company?

Mr. RIPLEY. Of a single issue.

The CHAIRMAN. Do you desire to make any comment on what kind of an investment it is?

Mr. RIPLEY. The primary comment I should make on it is that it is not suitable for people of small means, because it has not the attribute that such things ought to have, instant convertibility. That is what the savings banks offer. If you break your leg or lose your job, you can get the money back. There should be an open market for any security that is widely held. And the pathetic thing is that very large amounts of money at the present time, by these sales campaigns are being withdrawn from savings banks in order to be devoted to this other kind of investment.

The CHAIRMAN. Has it a promise of a great return?

Mr. RIPLEY. A very much greater return.

The CHAIRMAN. A very much greater return?

Mr. RIPLEY. These bonds which I have in mind are offering 8½ per cent at the beginning. They are in \$10 denominations, with only \$3 paid down. I invite your attention to the bookkeeping and handling charge, \$40,000,000 in \$10 lots, and ask you to consider who is going to pay those charges through rates on light and power.

In addition to the partial payment arrangement, there are all sorts of participation rights; rights to exchange, warrants, and so forth; together with the advantage that you will be allowed to deduct, or that there will be deducted for you, the amount of income tax in the State where you happen to live. Now is it possible to do all that with respect to \$40,000,000 worth of bonds?

The CHAIRMAN. And that was Associated Gas & Electric?

Mr. RIPLEY. Associated Gas. I do not know, in fact, and nobody can know, how sound that company is in and of itself. It is one of

those blind pools, so far as accounts are concerned, in which you trust your investment to somebody else.

That is what the people did in Chicago, and now they discover that all of the facts were not disclosed to them. I want all corporate facts spread on the record so that he who runs may read. You could contribute nothing else by law which would further stabilize conditions.

And, furthermore, you would not meet the opposition of the best and most soundly financed companies. I am trying to interest the industry in this direction, as I told Senator Glass's committee, and I have the promise of six or eight public utility leaders that they would not oppose the proposition. There was put into the record at that time a report which President Gifford, of the American Telephone & Telegraph Co., had prepared. It stated that the American Telephone & Telegraph Co. had not been prejudiced by enforced publicity of accounts; but that they found it worked to their advantage in two ways; first, when they had to raise new capital, immediately the books are opened, every one may know what the situation actually is. If they want to borrow a certain amount of short-term money the bankers may get in touch with the Interstate Commerce Commission and know precisely how things stand.

Senator FLETCHER. Do those people you speak of furnish a statement of their assets, their business, and their earnings, when they are selling these bonds?

Mr. RIPLEY. After a fashion, but who knows with certainty? All the Insull companies furnished statements.

Senator FLETCHER. Do they set forth what their purpose is in raising this \$40,000,000?

Mr. RIPLEY. Yes; I will read you—

Senator FLETCHER (interposing). Is it to go into their development, or expansion, or what?

Mr. RIPLEY. This is a circular of Associated Gas & Electric Securities Co., April 7, 1932:

Since the offering of 8½ per cent 8-year gold bonds was made, stockholder customers throughout the territory served, and other security holders, have purchased these bonds at the rate of nearly \$1,000,000 a week. Approximately \$5,000,000 of bonds have been already sold on the installment basis.

Now, in mentioning that company I am using it only as an illustration of the way in which popular investment in small lots is spreading at the present time, in order to impress on your minds the desirability of taking action without waiting too long.

The CHAIRMAN. Mr. Stock wants to ask you a question.

Mr. STOCK. Mr. Ripley, I do not know whether you are familiar with advertisements of Associated Gas running in the newspapers of about a year ago. These showed, as I remember it, two charts with an upward trend, one of the gross revenues, and the other of power output, giving the distinct impression that the company was progressing during the depression, as contrasted to other companies in the same field.

Mr. RIPLEY. Quite inevitably, the amount of money that goes into construction account—

Mr. STOCK. What I meant was that they had those two lines only, one of which showed the gross revenues and the other the kilowatt-

hours, the output. Now, the reason that they were going up all the time was because they were continually acquiring additional properties with the money which they were getting all the time from the people they sold their securities to.

Mr. RIPLEY. Yes; you can increase earnings any time if you sell enough securities to keep on buying more properties.

Mr. STOCK. To my point there is, do you not think that was a gross fraud and misstatement?

Mr. RIPLEY. I think it is open to that suspicion. A curve of gross revenues only was published, without indication of the attendant fixed charges incurred in raising new capital.

The CHAIRMAN. In other words, it was made to look like a good business when it was not.

Mr. RIPLEY. In connection with the work I am doing at Cambridge, we have taken sample periods, say a month at a time, and have tabulated the amount of advertising in the newspapers, applying the standard rate for advertising. We computed in this instance of Associated Gas & Electric that they are spending not less than \$1,000,000 a year for newspaper space; not to get people to buy electric refrigerators or service, but to get people to buy stocks and bonds.

Senator FLETCHER. Do you think now, Professor, that this buying and dealing in stocks and bonds is going on now to a considerable extent, even in these depressed times?

Mr. RIPLEY. Nothing like what happened in 1929. Many of the great sales organizations have disbanded because there is nothing to sell. I speak very feelingly there, because of the college men who have taken employment as stock and bond salesmen.

Senator FLETCHER. You mean to say this bond speculation has fallen off very considerably?

Mr. RIPLEY. My impression would be that outside of the group of people who do nothing else in and around Wall Street, the public participation was practically stopped. The people have not got the money.

Senator FLETCHER. I thought you were showing by the talk of these bonds that the disposition of the public was to continue.

Mr. RIPLEY. Well, they have got these utility securities for keeps, because there isn't any open market for them. The banks will not lend you money on them, because they have no dependable market value.

Mr. STOCK. These bonds of Associated Gas are selling now at 8½ per cent?

Mr. RIPLEY. The statement indicates that the base return is about 8½ per cent.

Mr. STOCK. I saw an analysis a few days ago, that all of the issues of better rank are selling for more than that, anywhere from 10 to 12 per cent, so that a person could walk out into the open market and buy them for less than that 12 per cent.

Mr. RIPLEY. One of my colleagues was solicited by a salesman to buy one of these securities at a price of \$85. We immediately looked up the quotations in case this had to be sold. We could not find a listed sale for three months, and the price at that time was something under 40. So the person who was persuaded to buy at 85, supposing he had to cash in on it, the most he could get was \$30 or \$40.

Senator TOWNSEND. Doctor Ripley, are you familiar with the effort to sell the Government baby bonds to the public?

Mr. RIPLEY. I do not know about that.

Senator TOWNSEND. You understand it was not successful?

Mr. RIPLEY. I do not know at all.

Senator TOWNSEND. I was just wondering why the people refused to buy the Government baby bonds and bought these others.

Mr. RIPLEY. These Associated bonds were advertised as baby bonds, and they were offered coincidentally through a great body of salesmen throughout the country.

Senator WALCOTT (reading circular). They have a new wrinkle here. They say that "the legality of these bonds will be passed upon by Messrs. Travis," and so on. So after they have sold them, they guarantee that they may be sometime passed upon. This sounds like a swindle. They show here what they say they have by a consolidated statement. It looks like a swindle on the face of it.

Mr. RIPLEY. Well, I do not know. But with all these figures, it is utterly confusing. It makes it impossible for anybody, no matter how skilled an analyst he may be, to make a comparison of one corporation with another.

Senator FLETCHER. It is a matter of interest. Senator Townsend's question was why they did not buy the Government bonds. They do not pay as much interest.

Mr. RIPLEY. If you want to bother with it, this statement will bear me out as respects the complexity of the corporate set-up. When this issue was first offered it was by Associated Gas & Electric Co., which is the holding company at the top. They were advertised as "baby bonds, guaranteed." Now the guarantee was by whom? The guarantee was by Associated Gas & Electric Corporation, every dollar of the stock of which was owned by other company at the top.

The CHAIRMAN. That is, were the bonds a first lien on any property?

Mr. RIPLEY. They were not in any event. Nor did the guarantee mean anything, because it was by a corporation 100 per cent owned by the other corporation. It is exactly as if I borrow money at the bank and get my son to guarantee payment when his only income is from me.

Senator WALCOTT. Like one pocket in your breeches guaranteeing the other.

Mr. RIPLEY. It would not be possible to do that if all these companies were forced to make full disclosure.

Senator WALCOTT. But there are all the figures, and nobody reads them. I am beginning to think, from the hearings we have had here, that what fools the public is these tremendous campaigns of selling, instituted, as we found a week ago, by the National City Bank, in which the officers and directors of the Anaconda Copper were interested, and then if they have anything left over that is sticky, they get the National City Bank to organize another pool, buy 200,000 additional shares and sell it to the public.

Mr. RIPLEY. Better than that, you may have an investment trust, and you put what you have left over in your investment trust.

Senator WALCOTT. But here is a great bank that puts up the money for its affiliate, which, in turn, places the stock on the market,

selling it out to the customers who have to take it to keep on the affiliate's list.

Mr. RIPLEY. There is no question about that.

Senator WALCOTT. Now, that leads to what the chairman asked you a little while ago: Is it not justified to have some kind of a Federal regulation that will prevent officers and directors of corporations speculating in their own stock?

Mr. RIPLEY. That is one of the most infamous things in the situation to-day. The statement of a man like Percy Rockefeller, director of a number of corporations, in stating to you that his major interest in those companies was buying and selling stocks, getting in and out of them was outrageous.

Senator WALCOTT. And the man who was helping him to run the pools was a specialist on the stock exchange. You can not beat that.

Mr. RIPLEY. But my proposition is that we most need publicity. The stock exchange is doing the best it can. They have their own experts. If they see that a security was being blown up unduly, they begin to check upon it.

Senator WALCOTT. England goes a step further, and Berlin used to; it has a fortnightly statement. That prevents a lot of speculation. I am inclined to think we have got to come to something like that.

Mr. RIPLEY. I think so.

Answering your question, Mr. Chairman, suppose it were part and parcel of corporate publicity that once a quarter all directors in these corporations should be compelled to disclose the number of shares they own directly or indirectly. Now, they could evade such a law with all kinds of fictitious names. But you could impose a heavy penalty on, making it so dangerous that they would not dare to conceal. In the older days when a man owned a little property in his own business, he was there forever. He slept with it. If it went, his whole fortune disappeared. What happens in the present day? The officers of the corporation are merely taken on as receivers. Their salary goes on just the same. It is a completely different system we are facing at the present time from the one which our fathers created. We have not even attempted to deal with it as we should.

May I say here, sir, that there is presently to be published a book to which I would like to direct your attention. It strikes at this whole business in a way different from anything else in print. It is a book by Prof. A. A. Berle, jr., of the Columbia University Law School. He is an eminent lawyer, as well as a student of social affairs. This is a large volume which will deal with these problems concerning popular investment. The title of the book, is *Private Property and the Corporate System*. It should have a profound influence upon legislation, because he brings to the front and makes evident by all sorts of concrete data, that we are living in a different world than that which existed before the war.

The CHAIRMAN. It is getting late, and I am sure the Senators would like to leave, and we will have to bring this to a close very soon. But I would like to ask you a few questions.

Do I understand it is a general practice among business men to add all the expense of advertising to the expense of production and charge it to the consumer?

Mr. RIPLEY. Yes; as a part of the operating expenses of the corporation.

The CHAIRMAN. So if it is necessary to sell more stock the expenses of that are added to the consumer?

Mr. RIPLEY. Yes, sir.

The CHAIRMAN. As a part of his light bill?

Mr. RIPLEY. Yes. Who else will pay for it? And that is why under these financings involved at the present time the cost of raising capital, which is so extraordinarily high, and must be so, adds a large item to operating expenses. The consumer has got to pay for it in the long run. We have a right to know how much it all costs as well as what the proper return thereon should be.

The CHAIRMAN. You have said something about several witnesses here. You have not said anything about Mr. Whitney's testimony. Did you go over that, too?

Mr. RIPLEY. I have read his testimony. I am less interested in the prevention of short selling than in these more fundamental problems. Speculation is just as vicious when it runs the other way.

Senator WALCOTT. It is the marginal buying—

Mr. RIPLEY (interposing). It is marginal buying, and all such business which does the mischief. But if you let the light in upon these transactions, through the accounting publicity which I have recommended, there are many people who will help to correct the undue fluctuation of prices through understanding transactions in such stocks and bonds.

The CHAIRMAN. Mr. Stock wants to ask another question.

Mr. STOCK. Mr. Ripley, I had a definite impression when I heard Mr. Mitchell testify. I had read countless letters from many people who had bought stock, and I had read the interoffice correspondence over Mr. Mitchell's name urging them to sell various securities, and his explanation of that, and to my mind his whole testimony, and the essentials of it can be put in one sentence, that he thought he had to use the same methods in selling investments that you do in selling carpets. That came from him as head of one of the biggest banks in the world. Do you care to make any statement in regard to that?

Mr. RIPLEY. I think there is too large a cost in selling. A cardinal rule with me is never to buy anything which anybody wants to sell me very badly. The entire organization of great sales companies affiliated with great banks, ought to be abolished by law.

Senator WALCOTT. The affiliates?

Mr. RIPLEY. The affiliates. Banking is one thing, and investment is another. The two should be rigidly set off from one another.

The CHAIRMAN. If there is nothing further, the committee will adjourn to meet on Thursday morning on the stock exchange investigation.

(At 12.45 o'clock p. m., the committee adjourned to meet on Thursday, June 16, 1932, at 10 o'clock a. m.)