Statement of Cyrus Eaton
Before the SEC Subcommittee
Of the Committee on Banking and Currency
of the U.S. Senate,
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A PROPOSAL TO MAKE INVESTORS' FUNDS AVAILABLE TO OUR EXPANDING ECONOMY BY REMOVING THE STRAIGHT JACKET OF OPPRESSIVE SEC REGULATION FROM THE CAPITAL MARKETS

My name is Cyrus Eaton. My business address is 2000 Terminal Tower, Cleveland, Ohio, and my residence is Acadia Farms, Northfield, Ohio.

As industrialist, banker and farmer, I have constant relationships with departments and agencies of the Federal Government. From my close personal knowledge of the Securities and Exchange Commission since its inception some fifteen years ago, I should today like to present to this Committee my views on Senate Bill 2408 to amend the Securities Exchange Act of 1934.

The SEC's Supplemental Report of January 9, 1950, like the original Report of June 19, 1946, is artfully labelled "A Proposal to Safeguard Investors in Unregistered Securities". A more appropriate title would be "A Proposal to Increase the Business of the New York Stock Exchange and to Expand the Hamstringing Activities of the SEC".

The New York Stock Exchange has been operating at a loss. The Big Board would therefore welcome with open arms the additional listings that most certainly would come its way on passage of the proposed legislation. So Senate Bill 2408 has the unstinted blessing and support of the Big Board and its business-hungry brokers, as well as the powerful law firms and publicity agencies that act as their master minds.

The Stock Exchange is looking for a new President, and it is no coincidence that the two candidates under most active consideration for the $75,000-a-year post are James J. Caffrey and Edmond M. Hanrahan, both former Chairmen of the SEC who left the Commission for lucrative private law practice in Wall Street. The Big Board figures that it will be all set with Senate Bill 2408 on the books and with a President who has an inside track with the SEC.

SEC Regulations Are A Threat to Initiative and Accomplishment

The SEC's eagerness for passage of this Bill to extend its powers is as readily understandable as its recent decision to postpone indefinitely the presentation to the Congress of measures to simplify the Securities Act of 1933 that have been under deliberation for a decade. As Senator Paul Douglas said about the bureaucrats, "No pressure group is more persistent or more skilled in the technique of getting what it wants. And in common with the others, it always wants more, and more, and more." And as Senator Douglas concluded, "...if they got all the money they want, approval of all their plans and authority to carry them out, government as we have known it in this free country would disappear. Enthusiasm, initiative, accomplishment would be suffocated under a mass of regulations..."

In this year when concern for the taxpayer and economy in government constitute the keynote of Congress, it would seem singularly inappropriate for the SEC to be embarking on a new regulatory venture that would require additional personnel and funds.

To believe the SEC's original and supplemental reports on the Bill under consideration, one would have to assume that the officers and directors of all corporations have no other aim in life than to defraud their stockholders, and that only by registration with the SEC can corporate officials be kept honest. This is, of course, sheer nonsense. America owes its industrial might to the men of management, no matter how much the SEC may malign them, and no report ever filed with the SEC ever added one cent to any stockholder's equity. For examples of the harm that may come to investors from reports required by the SEC, I should like to refer you to an illuminating analysis of the proposed legislation by Senator James E. Murray in the July 4, 1946, Commercial and Financial Chronicle.

Stockholders Do Not Yearn for Benevolent and Expensive SEC Intervention

Looking over the roster of companies studied by the SEC in the preparation of its Supplemental Report, I was interested to find the name of The Sherwin-Williams Co., of which I have been a director for a quarter of a century. This Cleveland institution, which has been in business almost 85 years, is the world's largest and most successful paint manufacturer. Its financial policies are conservative, and its securities are in the blue-chip class. Sherwin-Williams has been frequently importuned by New York Stock Exchange houses to list its securities on the Big Board, but has always declined. Despite the SEC's ardent desire to dictate to the Sherwin-Williams management, the 5,000 satisfied common and preferred stockholders

of this great Cleveland company are not yearning for the benevolent, and expensive, intervention of the Commission on their behalf.

I am also a director of another venerable Cleveland company, whose securities are listed on a national stock exchange and are therefore registered with the SEC. This is the 100-year old Cleveland-Cliffs Iron Co., the nation's leading independent iron ore company. Four years ago, we undertook to bring about a simplification of the company's capital structure by a union of the company with its wholly owned subsidiary. It took six months' of agonizing work on the part not only of the company's own personnel, but also an imposing battery of costly outside legal and accounting talent, to work out a procedure satisfactory to the SEC. The resultant proxy statement ran to the unbelievable total of 89 pages, which assuredly not one stockholder in a hundred read even in part. The expense per shareholder of the outside legal work alone I estimate at approximately $10, and I am willing to wager the more than $100,000 involved that each shareholder would have preferred to receive a ten-dollar bill instead of the SEC-prescribed proxy statement.

SEC Regulations Have Depressed Securities Values

One of the SEC's claims for the proposed legislation is that it may "spur legitimate investment in equity securities." The spuriousness of this contention is illustrated by the give-away prices at which many stocks long listed on national exchanges and registered with the SEC are selling in the market today. As examples, consider two more old Cleveland

industrials, National Acme Co. and White Motor Co. Their stocks, which are traded on the Big Board in New York, have a market value substantially less than their net quick assets. In other words, the market place puts less than no value on the physical properties and facilities of these great manufacturing companies, one the builder of vital machine tools and the other the maker of important heavy trucks.

Suppose that some merchant of securities considered that National Acme and White Motor stocks were bargains, and decided to buy blocks of them for redistribution to investors. If, in the process of the securities dealer's buying, the market on these securities advanced slightly, as doubtless would happen, the SEC would promptly accuse the dealer of committing a crime and would threaten him with imprisonment.

SEC Powers Need Curtailment Rather Than Extension

The SEC has cited the piece-meal fashion in which federal securities regulation was built up, from 1933 through 1940, as a reason why Senate Bill 2408 should be adopted. My own view is that this is a reason for a complete Congressional overhaul and simplification of all securities legislation before any extension of the SEC's powers is considered. The 8 pieces of legislation which, over the 8-year period, were successively urged upon the Congress under the pretense of protecting the investor, have instead acted as a straight jacket on the capital markets.

As matters now stand, none but the largest and strongest corporations can readily register securities with the SEC and get them cleared

for offering to the general investor. Access to the capital markets has been practically denied to the medium-sized and smaller companies.

Take the $2,749,820,215 of bond and debenture issues registered with the SEC and cleared for cash sale to investors in the Commission's fiscal year ended June 30, 1949. The mammoth Bell Telephone system, 14 giant electric and gas companies and 8 other huge corporations accounted for $2,025,821,178 of this debt financing. At the other end of the scale, only 5 bond issues of less than $1,000,000 were cleared for cash sale by the SEC. In other words, only 5 companies with financial needs in this relatively modest category were willing to endure the elaborate and expensive ordeal of SEC registration. This is appalling in a nation of 425,000 corporations, most of which ought to be expanding with our growing population.

Free From SEC Interference, Municipal Financing Flourishes

By way of contrast, consider the field of municipal finance, with which the SEC is barred by statute from interfering. During the same twelve-month period, 5,466 municipal issues aggregating more than $4,000,000,000 were sold to the public for cash. Had the communities that sold their bonds been forced to submit to the SEC's red tape, most of them undoubtedly would have been unable to raise the funds they needed.

Also, by way of contrast, consider the $10,000,000,000 a year that the people of the United States now gaily risk on bingo and other kinds of betting, without let or hindrance from the SEC. If these funds could be channeled into venture capital investments to increase the productivity of our mammoth industrial machine, an abundance of the good

things of this life would be assured to all Americans.

Senate Measures To Finance Small Business Bypass the SEC

The Senate has given ample evidence that it is alert to the financial needs of smaller business. In the last ten days alone, Senator Scott Lucas has introduced a bill to permit broader RFC lending to small enterprises, while Senator Joseph C. O'Mahoney has sponsored a measure to set up 36 regional banks to help small business financially. One is struck first by the fact that both of these proposals completely bypass the SEC, and second that, commendable as their purpose is, they would be unnecessary if the Congress would remove the straight jacket of oppressive SEC regulation from the capital markets.

On the first day of these hearings, the SEC suggested that Congress authorize it to make a two-year study of trading in securities. A more fruitful study, which the Congress itself should make, would be the re-examination and revision of all of the federal securities legislation which I mentioned earlier. Among other aspects that should be considered are the many instances in which powers and functions of the SEC are a duplication of powers and functions of the state regulatory commissions. I understand that Senator Burnet Maybank raised a question whether Senate Bill 2408 might not in some respects amount to "an invasion of states' rights," and similar invasions have already occurred in the case of earlier legislation.

"Investor Has Not Been Protected, But Thoroughly Misled" By The SEC

In conclusion, I can find no better statement of the problem that confronts your Committee than the following observation of Senator Murray in his 1946 article:

"Instead of extending the Securities Exchange Act to cover a large number of unlisted corporations with a probable result of killing the natural and normal development of small business and the over the counter markets, Congress should examine and restate their intent in the original acts. Then they should have an unbiased commission investigate the workings of the administration of these acts and the effect on the national economy during the abnormal time thru which the SEC has lived. Has the Commission carried out the intent of Congress? Has the SEC done more harm than good? Has the administration of these acts created conditions in the capital markets comparable to prohibition in the liquor trades and with the Black Markets created by the OPA? After Congress has thoroughly investigated the workings of the SEC and how the investor has not been protected, but in many instances thoroughly misled, by this so-called 'protective' agency, it will easily understand the necessity for a complete revision of the existing statutes, rather than an extension of the power now being sought by the SEC."