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## The Pecora Hearings

In late October 1929, Wall Street was badly shaken by what later came to be known as the “Great Crash.” On Black Monday and Black Tuesday (October 28 and 29), the Dow Jones Industrial Average fell from 300 to 230, well down from its September 3<sup>rd</sup> peak of 381. It ultimately bottomed out at 41 during the summer of 1932.<sup>1</sup> By this time, hundreds of banks had failed, prices had dropped dramatically, U.S. real per capita GDP had fallen by approximately 30%, and the unemployment rate stood at over 20%.<sup>2</sup> Many blamed Wall Street for the onset of the Great Depression; and Franklin Delano Roosevelt, who ultimately won the 1932 presidential election by a wide margin, promised to enact strict regulations on the financial community and put “an end to speculation.”<sup>3</sup>

In 1932, the Senate Banking Committee began a much-publicized investigation of the nation’s financial sector. The hearings, which came to be known as the Pecora hearings after the Banking Committee’s lead counsel Ferdinand Pecora, revealed how the country’s most respected financial institutions knowingly misled investors as to the desirability of certain securities, engaged in irresponsible investment behavior, and offered privileges to insiders not afforded to ordinary investors. During the famous “Hundred Day” congressional session that began his presidency, Roosevelt signed two bills meant to prevent some of these abuses. The first law required companies to register new securities with the Federal Trade Commission (FTC) and to publish prospectuses with detailed information on their business ventures before they could offer new securities to the public. The second law established insurance for bank deposits and forced financial institutions to choose between investment and commercial banking.<sup>4</sup>

Roosevelt also believed that the government should play a more active role in the financial system by regulating national securities exchanges. In February 1934, the president urged Congress to enact such legislation, prompting the introduction of a bill entitled the Securities Exchange Act. If enacted, this bill would force all securities exchanges to register with the Federal Trade Commission, would curtail the size of loans that could be advanced to securities investors, and would ban a number of practices (such as short-selling) that were thought to facilitate stock manipulation. Additionally, the legislation would require that all companies with exchange-listed securities publish detailed business reports as frequently as the FTC desired and would subject any company or exchange deemed to be in violation of the act’s provisions to increased legal liability.<sup>5</sup>

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4 Professor David Moss and Research Associates Cole Bolton and Eugene Kintgen prepared this case. This case was developed from published sources solely as the basis for class discussion. Cases are not intended to serve as endorsements, sources of primary data, or illustrations of effective or ineffective management.

Wall Street, represented in particular by New York Stock Exchange (NYSE) President Richard Whitney, took a strong position against the Securities Exchange Act. Whitney quickly broadened the NYSE's internal anti-manipulation rules, in hopes of convincing Washington that stock exchanges could effectively police themselves without any government involvement. The NYSE president also warned of the potentially disastrous effects of the legislation, arguing that the publicity measures of the Securities Exchange Act would enable the FTC to control companies' business practices and would prove so onerous that companies might choose to delist their securities from formal stock exchanges. He insisted, moreover, that the bill would reduce liquidity in securities markets and could even bring about a mass liquidation of shares as the result of its high margin requirements.<sup>6</sup>

While Whitney launched his assault on the bill, the Pecora Committee conducted a public inquiry into stock price manipulation at the New York Stock Exchange. Pecora detailed an instance just a few months earlier in which speculators, unbeknownst to the NYSE management, had artificially driven up the price of shares in alcohol (liquor) companies. Furthermore, the Committee revealed that when the NYSE eventually conducted its own investigation into the matter, its final report concluded that nothing improper had occurred. Pecora claimed that this lax oversight by the NYSE confirmed that exchanges were incapable of adequately regulating themselves and therefore passage of the Securities Exchange Act was vital.<sup>7</sup>

Spectacular financial abuses, like those involving the stocks of alcohol companies, had been routinely uncovered by the Pecora Committee for more than a year, captivating the nation and helping to instill in citizens a strong desire for financial reform.<sup>8</sup> So when Richard Whitney was summoned to testify during the congressional hearings on the Securities Exchange Act in late February 1934, he had the tough task of trying to prove to citizens and congressmen alike that the proposed bill was too restrictive.<sup>9</sup> Would he be able to convince lawmakers that the Securities Exchange Act would impose overly burdensome regulations on exchanges and stifle American securities markets, or would his arguments fail to win over those who believed that strict regulations were exactly what financial markets required following the Great Crash?

## The Securities Market in the 1920s

During World War I, the U.S. government's massive Liberty Loan drives introduced large numbers of Americans to the idea of investing in bonds, a prospect that would have seemed foreign to many prior to the war. In 1917 and 1918, "the number of bond buyers in the United States increased from 350,000 to 25 million persons" as more and more citizens considered it their patriotic duty to purchase Liberty Bonds.<sup>10</sup> According to historians, these far-reaching wartime loan drives increased Americans' willingness to invest in securities, priming them for the 1920s market surge.<sup>11</sup>

Indeed, stock indexes boomed in the 1920s as a suddenly investment-hungry populace readily bought up a torrent of newly issued securities. Over the decade as a whole, more than \$28 billion in corporate debt securities were issued, far more than the roughly \$12 billion issued during the 1910s. The growth in corporate equity issues was even more dramatic, with the total value of common and preferred stock issues more than tripling from \$5.8 billion in the 1910s, to \$18 billion in the 1920s. Likewise, the total volume of stocks and the aggregate value of bonds traded on the floor of the New York Stock Exchange nearly tripled from the 1910s to the 1920s.<sup>12</sup> (See Exhibits 1 and 2.)

Helping to fuel this massive surge in investment were margin loans, which allowed investors to borrow heavily from their brokers (often as much as 75 – 90% of the total cost) in order to buy securities. To fund their customers' margin accounts, brokers, in turn, had to take out brokers' loans from banks or other lenders. As a testament to the rapid increase in margin financing during this

time, aggregate brokers' loans surged from \$7.6 billion in 1924 to more than \$26.5 billion just five years later.<sup>13</sup>

### *Security Affiliates and Investment Trusts*

Prior to the 1920s, commercial banks rarely participated in securities markets. Marked by a historic commitment to safe and conservative practices, and bound by state and federal legislation that barred them from partaking in any sort of "nonbanking" activities, commercial bankers tended to focus on their deposit and loan businesses. These bankers generally kept their institutions' funds out of corporate securities and left the origination of stocks and bonds to J.P. Morgan and Company and similar private Wall Street investment firms.<sup>14</sup>

However, amid the stock market boom of the 1920s, many commercial banks abandoned their traditional outlooks and established subsidiary companies known as security affiliates. While many commercial banks had long had bond departments, through which they had sold Liberty Bonds during the war, these new subsidiary organizations allowed bankers to circumvent the laws that forbid them from dealing in the full spectrum of stocks and bonds. Additionally, by establishing such affiliates, many banks could bypass restrictions on interstate branching. Whereas only ten nationally-chartered banks and eight state-chartered banks had security affiliates in 1922, 105 national banks and 75 state banks had securities-dealing subsidiaries by 1930.<sup>15</sup>

These security affiliates often acted as both investment houses and broker-dealers, not only helping to originate securities—by 1930, about half of all bonds were originated by banks' security affiliates—but also then facilitating customers' purchases of these securities.<sup>16</sup> To attract walk-in clients, the affiliates often set up shop on the ground floor. Additionally, these companies would advertise in the era's most popular magazines, touting the virtues of an investment portfolio.<sup>17</sup>

Companies known as investment trusts, which were relatively new to the U.S. at this time, also found a niche selling securities during the 1920s, particularly to smaller investors. Like mutual funds of today, investment trusts sold shares in themselves to customers and invested their income in a securities portfolio. These portfolios could either be fixed or actively managed and often included stocks, bonds, and sometimes even shares of other investment trusts. These investment companies experienced a tremendous rise in popularity during the decade, increasing in count from 40 to more than 750 from 1921 to 1929.<sup>18</sup>

### *Stock Market Manipulations*

Schemes aimed at controlling security prices were common during the 1920s, and so-called "stock pools" or "pool operations" were among the most widespread stock market manipulations of the era.<sup>19</sup> The classic explanation of such practices was later given by John Kenneth Galbraith:

The nature of these operations varied somewhat but, in a typical operation, a number of traders pooled their resources to boom a particular stock. They appointed a pool manager, promised not to double-cross each other by private operations, and the pool manager then took a position in the stock which might also include shares contributed by the participants. This buying would increase prices and attract the interest of people watching the tape across the country. The interest of the latter would then be further stimulated by active selling and buying, all of which gave the impression that something big was afloat. Tipsheets and market commentators would tell of exciting developments in the offing. If all went well, the public would come in to buy, and prices would rise on their own. The pool manager would then sell

out [the pool's shares], pay himself a percentage of the profits, and divide the rest with his investors.<sup>20</sup>

In addition, some observers argued that certain stock pools also engaged in outright fraud, reporting "false statements or fictitious trades" to help inflate stock values.<sup>21</sup>

"Wash sales" were a specific form of manipulation that pool operators used to create the illusion of increased market activity in a given stock. In this practice, a stockholder would sell his shares on an exchange, but would employ a broker working on his behalf to re-purchase the shares, typically at a slightly higher value. Thus, by essentially selling his shares to himself, the market actor generated the appearance of active trading and exerted upward pressure on the stock's price, which, in turn, attracted other market participants to the stock. So-called "matched sales" were identical to wash sales, except that the market actor did not sell shares to himself, but rather sold them to another actor with whom he was colluding. By continually buying and selling the same shares back and forth between themselves, the actors could again entice outside investors to the stock by effecting the appearance of elevated market activity.<sup>22</sup> Although these manipulative practices were recognized as fraudulent, they "were seldom detected or penalized by stock exchange officials" of the era.<sup>23</sup>

Unlike the preceding manipulations, "bear raids" sought the artificial depression of a stock's price. Through this practice, a group of market actors would engage in intense short-selling of a chosen stock, thereby applying downward pressure on its price. If the share price fell enough, many investors who held the stock on margin would receive margin calls. That is, those investors who had borrowed heavily to purchase the stock would receive calls from their brokers when the stock's price fell below a critical threshold. If the investors could not come up with enough money to cover their margin requirements, they would then be forced to sell off a portion or all of their shares, which, in turn, drove the stock's price down further.<sup>24</sup>

## The Senate Banking Inquiry: A Shaky Start

In early 1932, with the depression deepening and stock indexes continuing to fall, President Herbert Hoover demanded that the New York Stock Exchange enact measures to stop manipulative practices such as stock pools and bear raids. When the NYSE failed to take any substantive action, the president called on Republican Senators Fredrick Walcott and Peter Norbeck, each of whom sat on the Senate Banking Committee, to lead an investigation of manipulative stock practices. On March 4, the Senate officially authorized the inquiry and allotted \$50,000 for the investigation.<sup>25</sup>

### *The Committee Falters*

On rumors of an impending bear raid, Hoover urged the Banking Committee to begin formal hearings in early April. The Banking Committee convened an emergency session on April 8 and called NYSE President Richard Whitney to testify on April 11. The Committee chose an attorney by the name of Claude Branch to serve as its temporary lead counsel. Branch and the senators had little time to prepare for the inquiry, and Whitney captivated the audience during the inquiry's opening sessions.<sup>26</sup> Legal historian Joel Seligman later described the initial hearings:

For the first two days they were a near-total disaster. A smooth, haughty Richard Whitney was the lead-off witness. The self-confident stock exchange president dazzled the five hundred or so reporters and spectators jammed into the modestly proportioned committee room. Suavely he denied knowledge of a bear raid scheduled for the previous Saturday. Indeed, Whitney testified, "constant investigations have shown . . . bear raids [do] not exist."

Nor did short-selling have much effect on market prices, accounting as it did for less than 5 percent of all stock exchange transactions. If they wanted culprits to blame for the exaggerated price movements of the great bull market and succeeding crash, Whitney suggested they look at "the high-powered political agents of prosperity," who misled the country into a "state of mind that . . . thought poverty was about to be abolished in our country forever."<sup>27</sup>

The early hearings went so poorly that Senator Norbeck, the Banking Committee's chairman, replaced Branch with the lead counsel's assistant, trial lawyer William Gray. By the end of the month, the investigation began to gather momentum when it was revealed that a publicist had received nearly \$300,000 over a decade-long span to plant articles in respectable newspapers, such as the *New York Times* and the *Wall Street Journal*, which were aimed at increasing the share price of more than 60 different securities.<sup>28</sup>

In mid-May, after the Committee had returned from a brief adjournment, Gray revealed that the brokerage firm of M.J. Meehan and Company had earned \$5 million over the course of a single week in March 1929 by organizing a pool operation in Radio Corporation of America stock. He also demonstrated how various prominent investors had profited enormously through the exploitation of insider information and through securities-related tax evasion.<sup>29</sup>

While the Banking Committee's revelations graced the front pages of the nation's leading newspapers, Gray's handling of the inquiry frustrated a number of the Committee members. Gray could not substantiate his claims that some witnesses engaged in wash sales and other questionable stock transfers, and he failed to subpoena one particular witness who later escaped to Europe.<sup>30</sup> In June, Senator Norbeck struggled to secure \$50,000 to continue the investigation, and, to the public's surprise, the hearings officially adjourned on June 24. On the same day that the Committee declared the suspension of its inquiry, Norbeck announced that Gray's services would no longer be required.<sup>31</sup>

### *The Inquiry in Suspension*

During the summer and fall of 1932, President Hoover gave little indication that he wished to resume the Banking Committee's hearings. In fact, Hoover seemed to shun any federal involvement in securities markets, believing instead that securities regulation should be left to the states. Additionally, his reelection platform made no mention of stock exchanges. Democratic presidential nominee Franklin Delano Roosevelt, on the other hand, devoted several planks of his campaign platform to the reform of securities trading, pledging to enact sweeping federal legislation to regulate the industry if elected. The Democrat's platform ultimately resonated much more strongly among the nation's voters, and barely a week after Roosevelt's landslide victory in November 1932, Senator Norbeck announced that the Banking Committee's hearings would resume when Congress convened its short lame-duck session in early December.<sup>32</sup>

Norbeck, however, encountered difficulties finding a replacement for William Gray. He was turned down by his first three choices before a lawyer by the name of Irving Ben Cooper agreed to take the post on January 10, 1933.<sup>33</sup> A week later, Cooper resigned, claiming in a letter that was published in the *New York Times* that Norbeck had violated an agreement to grant him "a free hand in the conduct of the investigation."<sup>34</sup> On January 24, Norbeck announced that Cooper would be replaced by Ferdinand Pecora. The Sicilian-born lawyer had been recommended to Norbeck by former New York District Attorney Joab H. Banton, who praised Pecora as "the best qualified lawyer in the country" to pursue the investigation.<sup>35</sup> Although Pecora was known to be quite theatrical, he was also regarded as an adept cross-examiner. After the Cooper debacle, Norbeck assured the public that his new hire would "have all the authority necessary to make a comprehensive investigation."<sup>36</sup> Indeed, the new general counsel would play such a major role in the proceedings over the following

months that the Senate Banking Committee's investigative hearings became known as the Pecora hearings.

## The Hearings under Pecora

### *Insull Inquiry*

In mid-February, the hearings recommenced with Pecora's investigation of the so-called "Insull empire," a once massive group of utilities assembled by the British-born Samuel Insull, who had worked for a time as Thomas Edison's business and financial manager before striking out on his own to Chicago. At its peak in the mid-1920s, the Insull empire was the nation's third-largest consortium of utility companies, providing an eighth of the country's electricity.<sup>37</sup> In late 1931, however, shares in the Insull companies collapsed, with rumors of managerial ineptness and fraud hastening the empire's decline into insolvency. Hundreds of thousands of stock and bondholders were wiped out as a result, and the panic caused by the Insull crash led to runs that closed 25 Chicago-area banks. The Insull name, consequently, came to be widely reviled.<sup>38</sup> In the run-up to the 1932 election, Roosevelt had harshly criticized Samuel Insull and denounced the entire power industry as "evil."<sup>39</sup> At one particular campaign event, while condemning the selfish and monopolistic practices of industrial and financial barons, Roosevelt referred to "the lone wolf, the unethical competitor, the reckless promoter, the Ishmael or Insull whose hand is against every man's."<sup>40</sup>

Samuel Insull absconded to Greece in 1932 after learning of a pending federal indictment, prompting the Banking Committee to interview his son, Samuel Insull, Jr., instead. With the empire's heir on the stand, the Committee attempted to demonstrate that the Insull family had used its privileged position to take advantage of its companies' shareholders. Specifically, Pecora revealed that Insull family members had signed a contract giving them the option to purchase more than 1.2 million shares in the Insull Utility Investment Company for less than \$12 million at a time when their value on the exchange was over \$36 million. Insull, Jr. defended his family's actions, claiming that the contract had been made at an earlier date and simply went unsigned for some time, and that nobody had expected the stock price to appreciate as it did.<sup>41</sup>

In addition to probing the family's questionable dealings in company stock, Pecora targeted the Insull consortium's notoriously convoluted organizational structure. The testimony of Owen D. Young, who served as chairman of General Electric and was one of the Insull companies' creditors, proved especially revealing:<sup>42</sup>

[The Insull group consisted of great] numbers of operating utilities, with holding companies superimposed on the utilities, and holding companies superimposed on those holding companies, investment companies and affiliates, which made it, as I thought then and think now, impossible for any man, however able, really to grasp the situation. . . . And if I may add: I should like to say here that I believe Mr. Samuel Insull was very largely the victim of that complicated structure, which got even beyond his power, competent as he was, to understand it. . . . [I]f I am right in thinking that Mr. Insull himself was not able ultimately to understand that structure, how can the ordinary investor . . . be expected to know, or even to inform themselves, conscientious and able as they might be, really as to the value of those securities?<sup>43</sup>

The highly fragmented structure of the utility empire allowed the Insull family to creatively bypass lending laws. By having their myriad companies borrow relatively small sums from a number of

Illinois' biggest banks, the Insull group was able to evade a state law that prevented banks from lending more than 15% of their total capital and surplus to any one entity. That is, while no single Insull firm borrowed more than the 15% limit from any bank, certain individual banks' aggregate lending to all Insull-controlled companies far exceeded the statutory ceiling.<sup>44</sup>

The Committee also revealed major accounting irregularities, including multiple occasions in which Insull firms recorded profits in their annual reports, but reported losses on their official tax filings. Additionally, the Committee drew attention to the actions of Halsey Stuart, an investment bank which owned large caches of Insull securities and which shared many of its directors with Insull firms. Halsey Stuart, Pecora asserted, had used stock pools to maintain Insull company shares at inflated prices.<sup>45</sup>

### *National City Inquiry*

After finishing its inquiry into the Insull empire, the Banking Committee commenced a headline-grabbing examination of National City Bank and National City Company, the latter having been established as a security affiliate of the former in 1911. During the booming 1920s, National City Bank had been the largest bank in the nation, while National City Company had been "reputed to be the world's largest distributor of securities," averaging \$1.5 billion in annual securities sales at the height of its business.<sup>46</sup>

Pecora began the inquiry with a detailed questioning of Charles E. Mitchell, who, as chairman of National City's board, presided over both the Bank and the Company.<sup>47</sup> The first few days of the hearings produced shocking revelations that *Time* magazine called the "Damnation of Mitchell." The Banking Committee revealed that Mitchell had received the then astounding sums of \$1,081,230 in 1927 (approximately \$13.4 million in 2008 dollars), \$1,341,634 in 1928 (\$16.8 million), and \$1,133,868 in 1929 (\$14.2 million). Additionally, Mitchell came under heavy scrutiny for selling 18,000 shares in National City to his wife during the market crash. In so doing, Mitchell established a \$2.8 million (\$35.1 million) capital loss, which, in spite of his significant earnings, allowed him to avoid paying income taxes for the year 1929. The media feasted on these disclosures and Mitchell quickly became the foremost scapegoat of the inquiry. Just five days into the National City hearings, Mitchell tendered his resignation, allegedly on the urging of then President-elect Roosevelt. Within a month, the former Wall Street titan was indicted on charges of income tax evasion.<sup>48</sup>

Mitchell, however, was not Pecora's only target. The lawyer went on to attack all of the high-ranking officers of National City for their excesses, revealing that a "morale loan fund" had been established by National City in the weeks after the initial market crash.<sup>49</sup> Through this fund, roughly 100 of National City's officers borrowed \$2.4 million of the firm's money to help them cover personal losses stemming from the market downturn. These officers did not need to pledge collateral to obtain such funds and their loans bore no interest. By the time of the hearings, "[o]nly about five per cent of this money had been repaid" and National City had made no efforts to collect the remainder, simply writing much of it off as a loss.<sup>50</sup>

In addition to disgracing National City's officers, the Banking Committee attempted to demonstrate that National City Bank and National City Company were "inseparably interwoven" and thereby violated laws dividing commercial banking and investment banking functions.<sup>51</sup> Pecora revealed that the very same stockholders that owned the Bank also owned the Company; in fact, the Bank's and the Company's stock certificates were printed on the opposite sides of a single piece of paper. Additionally, Pecora disclosed that the Company's initial capital had been quickly and easily obtained through the declaration of a one-time 40% dividend on the Bank's stock, and that all voting

power in the Company was vested in three trustees, each of whom served as a director or officer at National City Bank.<sup>52</sup>

To highlight National City Company's high-pressure sales tactics, Pecora called witnesses, including ordinary investors, to testify before the Banking Committee. Questioning revealed that National City representatives had persuaded clients into taking on sizable loans to facilitate larger purchases, that many agents had actively dissuaded customers from cashing out, and that the Company had vigorously pushed certain securities in which it had a particular interest. Indeed, the Company applied especially strong pressure on its customers to buy stock in National City itself, selling nearly 2 million shares in its parent company (totaling some \$650 million) from mid-1927 to the end of 1930.<sup>53</sup> Pecora also showed that National City Bank depositors were specifically targeted and solicited by Company sales representatives, and that the management of National City aggressively encouraged agents to sell as many securities as possible—particularly those that were slumping, riskier, and harder-to-move—by making subtle threats on agents' job security and by holding frequent competitions that offered cash prizes to top sellers.<sup>54</sup>

The inquiry also revealed numerous instances in which National City Company had willfully withheld pertinent information from its clients regarding certain securities that it offered. The most dramatic example occurred in 1927 and 1928, when National City Company helped sponsor and market \$90 million in Peruvian bonds in spite of repeated internal reports acknowledging that the country suffered from political instability, an unfavorable balance of trade, a poor credit history, and significant budget problems. The Company's bond prospectuses, however, made no mention of Peru's adverse economic conditions. Within a few years, the entire issue of Peruvian bonds had gone into default, costing bondholders some \$75 million by early 1933.<sup>55</sup>

Pecora further demonstrated that National City Company had engaged in pool operations (though company officials used more euphemistic terms such as "joint accounts") to prop up the price of particular securities in which it had a strong interest. Additionally, the Company was shown to have traded heavily in National City Bank shares. Although banks were expressly forbidden from trading in their own stock, because National City Company was a security affiliate of National City Bank, such dealing effectively skirted the law.<sup>56</sup>

The Banking Committee also accused National City of offering special privileges to insiders that were not available to normal investors and shareholders. Pecora showed that National City Company had purchased a large quantity of the newly organized Boeing Corporation's shares in 1928, but instead of passing the stock on to the public as in normal investment banking procedure, National City distributed shares at favorable prices to an assortment of its "officers, directors, key men, and special friends."<sup>57</sup> When Boeing stock began trading on exchanges soon thereafter, prices immediately surpassed the rates paid by the firm's "special friends." Many, including the National City Company itself, made handsome profits. Additionally, the Banking Committee highlighted an instance in 1931 in which National City Company, just weeks after underwriting a \$66 million issue of bonds on behalf of the Port Authority of New York, extended an unsecured \$10,000 loan to the Port Authority's general manager. By the time of the inquiry, Pecora noted, none of the loan had been repaid.<sup>58</sup>

Finally, Pecora showed how National City Bank used its security affiliate and its shareholders to bail itself out of bad loans. Amid a boom in sugar prices during World War I, the Bank had lent significant sums to Cuban sugar firms. When sugar prices plummeted in the early 1920s, however, the Cuban firms proved unable to pay back their loans. In response, National City called on its shareholders to purchase \$50 million in new stock. The shareholders complied, and the Bank and the Company evenly split the newly raised capital. Immediately, the Company used its \$25 million capital increase to buy every share in the newly created General Sugar Corporation. This new



corporation, entirely controlled by National City Company, used its \$25 million capital injection to purchase the bad Cuban sugar loans from National City Bank. Eventually, the Company wrote down the value of its General Sugar holdings to \$1, effectively realizing a \$25 million loss on this investment. Of course, the investment was never intended to make money for the Company or its stockholders; rather, it was a calculated plan by which the Company was able to erase what would have been a serious point of concern—the imprudent loans to Cuban sugar companies—from its parent bank's balance sheets. At the time of the \$50 million stock issue, investors were completely unaware of the chicanery that the Bank and the Company planned to employ, as National City opted not to inform shareholders of its true intent in raising the capital.<sup>59</sup>

## Financial Reforms of 1933

On March 4, 1933, just two days after Pecora finished his examination of National City, Franklin Delano Roosevelt was sworn in as president. In his inaugural address, Roosevelt decried “unscrupulous money changers” and promised to bring about “strict supervision of all banking and credits and investments.”<sup>60</sup> Indeed, with panicking depositors running on banks throughout the country, Roosevelt sprang into action, declaring a national bank holiday within two days of assuming the presidency. Roosevelt then publicly directed federal inspectors to scrutinize the finances of every single national bank in the U.S., pledging to reopen all those institutions that the inspectors deemed solvent.<sup>61</sup>

### *The Glass-Steagall Banking Act of 1933*

With Roosevelt's bank holiday underscoring the dire straits of the American banking industry, Congress reconsidered and ultimately passed a banking reform bill that had been repeatedly revived and revised since its initial introduction in January 1932.<sup>62</sup> This legislation, which was popularly referred to as the Glass-Steagall Act\* after its sponsors Senator Carter Glass and Representative Henry Steagall, reformed American banking in two major ways.<sup>63</sup>

The first of these reforms was the establishment of deposit insurance. A Temporary Deposit Insurance Fund, which was financed by contributions from member banks, was established on January 1, 1934, and provided \$2,500 in insurance per depositor (this level was soon raised to \$5,000 per depositor). Though slightly later than prescribed in the Glass-Steagall Act, this temporary entity was eventually replaced by the permanent Federal Deposit Insurance Corporation in 1935.<sup>64</sup> The banking legislation of 1933 and 1935 also provided for significant federal supervision of insured banks.<sup>65</sup>

The second major component of the Glass-Steagall Act of 1933 separated the deposit banking and investment banking industries. Specifically, the act gave national banks, such as National City, one year to break with their security investment affiliates, and barred the officers and directors of a commercial bank from acting as officers or directors of an investment bank. The act also required private banks, like J.P. Morgan and Company, to choose between their deposit banking business and their securities underwriting business, as they could no longer engage in both.<sup>66</sup>

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\* The Banking Act of 1933 should not be confused with the first Glass-Steagall Act passed in 1932. The first Glass-Steagall Act expanded the acceptable collateral that banks could post in order to receive Federal Reserve loans and also allowed the nation's money supply to be backed, in part, by Treasury securities. For more, see Milton Friedman and Anna Jacobson Schwartz, *A Monetary History of the United States, 1867-1960* (Princeton, N.J.: Princeton University Press, 1963), pp. 191, 321.

While Roosevelt praised the Glass-Steagall Act, which he signed into law on June 16, 1933, many in the banking community were highly critical of the new legislation. A number of detractors, including the president of the American Bankers' Association, attacked the act's deposit insurance provision, claiming that it would reward unstable banks at the expense of strong and solvent institutions. Other critics made broader arguments, claiming that the act was highly detrimental to the banking and investment industries and that it was "likely to slow up the recovery" from the ongoing depression.<sup>67</sup>

### *Securities Act of 1933*

Back on March 29, when the American public was still fuming over the disclosures of Pecora's National City inquiry, President Roosevelt presented Congress with his outline for new securities legislation, which he claimed would "give impetus to honest dealing in securities and thereby bring back public confidence."<sup>68</sup> Through such a bill, the president proposed to add to "the ancient rule of caveat emptor [let the buyer beware], the further doctrine 'let the seller also beware.'"<sup>69</sup> Over the next eight weeks, several versions of a securities bill were drawn up, debated, and revised.<sup>70</sup>

In its final form, the Securities Act of 1933, which was also known as the Truth in Securities Act, required issuers of new securities to file application papers with the Federal Trade Commission (FTC)<sup>\*</sup> and to publish prospectuses providing extensive details about their companies, including:

1. The names and addresses of all directors, high-level officers, and large shareholders<sup>†</sup>, plus details about their overall holdings of the company's securities and their stakes in the impending securities issue.
2. The amount of compensation received by each director, and the amount of compensation, if in excess of \$25,000 annually, received by each officer or other employee.
3. The names and addresses of those underwriting the issue of securities, and details about their stakes in the impending securities issue and their overall holdings of the company's securities.
4. Detailed information about the company's operations and business dealings, and detailed information about all of its outstanding securities and options.
5. Details on how the proceeds from the securities' sale were intended to be employed by the company, how the price was determined, and all compensation received by the issue's underwriters and promoters.
6. A recent balance sheet noting all assets and liabilities, along with a profit and loss statement.<sup>71</sup>

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<sup>\*</sup> Many types of securities were exempt from FTC registration, including all extant securities, all securities issued by banks and savings and loan institutions, all railroad securities, and all federal, state and local government securities. Other securities that had a repayment period of nine months or less, were issued intrastate, represented "insurance annuity contracts," and totaled no more than \$100,000 were also subject to FTC exemption. For more see, Joel Seligman, *The Transformation of Wall Street* (Boston: Northeastern University Press, 1995), p. 71.

<sup>†</sup> Large shareholders were those owning or with the option to own greater than 10% of the company's overall stock, or those owning or with the option to own greater than 10% of any single class of the company's securities. For more, see "'Truth in Securities' Bill Repassed by House, Senate," *Wall Street Journal*, May 25, 1933, p. 10.

According to the act, the FTC had 20 days to review the company's registration material before the firm would be allowed to offer its new securities for public sale, and the entire securities issue could be delayed if the FTC found any problems with the company's documentation. Also, the Securities Act contained stringent liability rules, allowing investors who discovered inaccuracies or material omissions in the FTC filing to sue all parties involved in the registration's preparation. In the event of such a suit, the act stated that the burden of proof would fall on the security-issuer and all other parties involved in the security's issuance to demonstrate that they had not intentionally misled investors. Finally, the Truth in Securities Act gave the FTC the power to enact standardized accounting guidelines, as variability in such methods had been a cause of much confusion over the years and had disallowed investors from easily comparing one firm's books to another's.<sup>72</sup>

### *Exchange Control?*

On the same day that he introduced the initial Truth in Securities bill in March 1933, Roosevelt made clear that he wanted to extend government regulation to include securities exchanges. However, Roosevelt also stated that his administration was "not yet ready" to propose such legislation.<sup>73</sup> Fearing an eventual regulatory bill, New York Stock Exchange President Richard Whitney asked to meet with President Roosevelt. At their meeting, Whitney attempted to convince Roosevelt that federal securities exchange regulations were unnecessary, stating that the NYSE was both willing and capable of policing itself. Whitney also tried to show that his organization's interests were actually in line with Roosevelt's, claiming that "the vast majority of the members of the Exchange are anxious to put the security business on a higher plane than it has ever been before."<sup>74</sup> Not long after the meeting, the NYSE enacted new internal regulations that required all trading pools and similar accounts to file weekly reports, imposed minimum balances on customers' margin accounts, and dissuaded securities distributors from engaging in aggressive sales policies. Nevertheless, it appeared that Roosevelt still favored federal regulation.<sup>75</sup>

### *Criticism and the Dickinson Committee*

Criticism of the Securities Act began immediately, and rose to a crescendo during the summer and fall of 1933. Detractors claimed that the law was too complex and that its liability rules were too harsh, making it virtually impossible for new companies to obtain startup financing and for existing firms to increase capital. Because of these restrictive effects on business, opponents argued, the law could potentially serve to exacerbate the ongoing depression. Some within the Roosevelt Administration also came to believe that the legislation needed to be revised, and Roosevelt responded by having two separate committees study the bill's alleged detrimental effects on securities sales. One of the committees, the so-called "Dickinson Committee," which was named after Assistant Commerce Secretary John Dickinson, was also charged with the additional task of drafting an outline for a new bill to regulate securities exchanges.<sup>76</sup>

## The Pecora Hearings Resume

### *J.P. Morgan and Company*

On May 23, 1933, just four days before President Roosevelt signed the Securities Act into law, the Pecora Committee commenced an investigation of J.P. Morgan and Company. The publicity generated by the Pecora hearings peaked during the inquiry into the House of Morgan, which *Time*

magazine had described as "the greatest and most legendary private business of modern times."<sup>77</sup> The company had traditionally kept a lower profile than other major Wall Street institutions, and its top partner, J.P. Morgan, Jr., had long avoided the public spotlight. Thus, when the scion of the House of Morgan was called to testify, droves of reporters and spectators flocked to the Senate Office Building, forcing the Banking Committee to move the hearings to a larger venue.<sup>78</sup> During the first day of Morgan, Jr.'s testimony, Pecora's questioning revealed that neither the banker nor any of his partners had paid income taxes for the years 1931 and 1932. In fact, because of major investment losses, many of the nation's wealthiest citizens earned no net taxable income during these years, a revelation which proved to be one of the most sensational of the entire hearings and prompted the *Washington Post* to print an article entitled "Rich Men Pay No Tax."<sup>79</sup>

Over the twelve-day inquiry, Pecora attempted to demonstrate that J.P. Morgan and Company's dealings had benefited insiders at the expense of ordinary investors and that the company had abandoned its exacting standards in order to capitalize on the market boom. Specifically, Pecora exposed how the company's use of "preferred lists" enabled well-connected investors to make enormous and immediate capital gains. On at least five occasions, J.P. Morgan offered stock to its firm members and other influential figures (including prominent national politicians and business leaders) at prices well below the prevailing market rates. For example, the company had given insiders a chance to purchase shares in the Alleghany Corporation for \$20 while such securities were trading at \$35 on the floor of the New York Stock Exchange.<sup>80</sup> Those lucky enough to be on J.P. Morgan's preferred lists could make an immediate profit by quickly selling the stocks on the exchange. Such preferred lists violated no laws, but their existence strengthened the perception that Wall Street insiders were given opportunities not available to ordinary investors.<sup>81</sup>

Although Pecora admitted that "the investigation of the Morgan firm elicited no such disclosures of glaring abuses" as those exhibited by other Wall Street firms, the public was still outraged by the secretive and disreputable, albeit technically legal, practices that the Morgan hearings had uncovered.<sup>82</sup> An editorial in the *New York Times* announced:

Here was a firm of bankers, perhaps the most famous and powerful in the whole world, which was certainly under no necessity of practicing the small arts of petty traders. Yet it failed under a test of its pride and prestige. By a mistake which had with the years swollen into a grievous fault, it sacrificed something intangible, imponderable, that has to do with the very highest repute. The members of such a partnership forgot that they must not only be beyond reproach in their financial dealings—as they doubtless are—but must always appear to be so.<sup>83</sup>

Some observers argued that the public's bitter reaction to the J.P. Morgan disclosures galvanized support for the Glass-Steagall banking bill, which the Senate abruptly and resoundingly passed amid the Morgan hearings.<sup>84</sup>

### *Chase National Bank*

After concluding its inquiry into the dealings of J.P. Morgan and Company, the Banking Committee investigated two more prominent investment banks, Kuhn, Loeb and Company and Dillon, Read and Company. In mid-October, however, Pecora turned his attention to Chase National Bank, which had overtaken National City in 1930 as the country's largest bank.<sup>85</sup>

Pecora revealed that Chase National Bank had established no less than five security affiliates, the most important of which was Chase Securities Company. Just like National City Company, Chase Securities Company was owned by the exact same stockholders as its parent bank, with the two

companies' stock certificates again "printed on reverse sides of the same piece of paper."<sup>86</sup> The Banking Committee showed that Chase Securities Company had conducted pool operations in a wide range of corporate stocks and foreign bonds during the late 1920s and early 1930s. Additionally, it was shown that the security affiliate had participated in at least eight pool operations in its parent bank's stock, which, Pecora argued, had helped drive Chase's share price from \$575 in the autumn of 1927 to \$1,415 two years later.<sup>87</sup> When former Chase Chairman Albert H. Wiggin was asked flatly why Chase Securities Company had decided to engage in such stock pools (Wiggin preferred the term "trading accounts"), he could only muster the response, "I think the times."<sup>88</sup> Shortly thereafter, Wiggin suggested that he "certainly would not do anything today that, if it turned out unfortunately, was going to be criticized."<sup>89</sup>

Much as he had done with Charles E. Mitchell, Pecora went on the attack with Wiggin. Pecora focused on the former chairman's income, showing that in addition to his compensation from Chase, Wiggin held 59 directorships in other firms, some of which paid him up to \$40,000 annually for his services. Many of these firms were also clients of Chase National Bank. Pecora highlighted a particular instance in which Wiggin, who served on a committee of the Brooklyn-Manhattan Transit Company, used his inside knowledge of Brooklyn-Manhattan's financial dealings with Chase to sell off his personal holdings of the transit company's stock while its share price was still high. Had he waited to sell his shares until knowledge of the company's dealings became publicly known, as a lay investor would have, Wiggin's sale would likely have netted less than half of what it actually did.<sup>90</sup>

Additionally, the Banking Committee went on to show how Wiggin had established six companies, either owned by himself or his immediate family, which seemed to do little more than speculate and engage in stock pools with money borrowed from Chase National Bank. Through these companies, Wiggin sold his own bank's stock short, resulting in a \$4 million personal profit in just a three-month period in late 1929.<sup>91</sup> Like Mitchell, Wiggin left the hearings in disgrace, having felt compelled by a "storm of popular disapproval" to refuse his \$100,000 annual pension from Chase.<sup>92</sup>

The shocking disclosures regarding Chase National prompted the bank's current chairman Winthrop T. Aldrich, who had already received stockholder consent to disaffiliate Chase Securities Company from Chase National Bank in May, to distance the firm further from Wiggin and the speculative practices of the 1920s. Said Aldrich, "as long as I have anything to do with the management, the market in Chase stock shall not be affected by the operation of trading accounts by the affiliates of the bank."<sup>93</sup> Aldrich backed his tough words by explicitly banning all of the bank's subsidiaries from engaging in pool operations in Chase stock.<sup>94</sup>

## The Proposed Securities Exchange Act

### *The Dickinson Committee Report*

In late January 1934, several weeks after Pecora finished up his examination of Chase National Bank, the Dickinson Committee released its official report on a new securities exchange bill. While the Dickinson group had previously announced that it was in favor of a bill that allowed exchanges to "discipline [their] own members and conduct their [own] affairs," the committee's formal report elaborated considerably on this initial sentiment.<sup>95</sup> Most notably, the report suggested the creation of a "Federal Stock Exchange Authority," either as an independent body or as a part of the Federal Trade Commission. The committee favored granting this new body the authority to study the securities industry further and make its own rules regarding pools, short selling, margin

requirements (in conjunction with the Fed), security listing requirements, reporting and accounting standards, and the role of exchange specialists.\* Additionally, the Dickinson group maintained that the Federal Stock Exchange Authority should be given adequate power to punish violators.<sup>96</sup>

While the Dickinson Committee wanted to leave much of the regulatory decision-making to the proposed Federal Stock Exchange Authority, the report did make a few specific recommendations, namely that all exchanges engaging in interstate commerce should be licensed by the federal government (licensure of over-the-counter exchanges and individual brokers, the committee stated, should not be required). Additionally, the Dickinson group advised that any new legislation should ban wash sales and matched sales, and should compel all companies with listed securities to take steps to increase their transparency, including requiring them to release quarterly reports and to submit to annual examinations of their books by independent accountants.<sup>97</sup>

### *Introduction of the Bill*

President Roosevelt disagreed with the Dickinson Committee's recommended approach, believing instead that a new securities bill should grant the government more explicit regulatory authority over the nation's exchanges. On February 9, 1934, the president wrote a message to Congress which briefly outlined his vision for a new securities exchange bill.<sup>98</sup> He stated:

The exchanges in many parts of the country which deal in securities and commodities conduct, of course, a national business because their customers live in every part of the country. The managers of these exchanges have, it is true, often taken steps to correct certain obvious abuses. We must be certain that abuses are eliminated, and to this end a broad policy of national regulation is required.<sup>99</sup>

After the president's statement was presented, Senator Duncan U. Fletcher introduced the National Securities Exchange Act of 1934. As written, the bill would deny all exchanges the right to use the postal system or to engage in any form of interstate commerce unless they registered with the Federal Trade Commission. Additionally, the act would prohibit margin lending on any security not listed on a registered exchange. Margin lending would be permitted on exchange-listed securities, but would be capped at the higher of two values: either 40% of the security's current price, or 80% of the security's lowest selling price over the previous three years. In addition, the act would impose an outright ban on all wash sales, matched sales, any actions aimed at artificially raising or lowering a security's price (e.g., pool operations and bear raids), the dissemination of rumors or other deceptive information about a security, any actions aimed at holding a security's price steady (unless the FTC was first informed about such actions), cornering a security (i.e., taking a controlling stake in a security with the intent of manipulating its price), the exercising of options (such as puts and calls) on securities, and the short selling of exchange-listed securities. The act would also impose strict civil liability rules on violators of the bill's provisions, allowing injured parties to file suit.<sup>100</sup>

In addition, Fletcher's bill would ban exchange members and brokers from both underwriting securities and dealing in securities on their own accounts. The act would also require the registration of exchange specialists and would prohibit these specialists from disclosing information that was not publicly available. Furthermore, the bill would require all listed securities to be registered with both the exchange and the FTC. Securities issuers would also be compelled to publish reports detailing their business on an annual, quarterly, and even monthly basis. The act would require that

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\* The Securities Exchange bill defined a specialist as "any person who specializes in the execution of orders in respect of any security or securities on an exchange and who commonly receives from other members of the exchange orders for execution in respect of such security or securities." See "Text of Bill for Regulating Stock Exchanges," *Wall Street Journal*, Feb. 10, 1934, p. 4.

exchanges, and all of those doing business on such exchanges, maintain detailed transaction records, which were to be made available for FTC inspection upon request. Additionally, the act contained a so-called "anti-Wiggin" rule, which would compel directors, officers, and major shareholders to disclose their dealings and holdings in their companies' securities and would forbid them from speculating in such securities. Also, the FTC would be empowered to revoke an exchange's or a security's registration if violations were discovered. Finally, the FTC would be given the authority to establish rules for over-the-counter (non-exchange-based) securities markets and be granted broad leeway to modify the abovementioned rules as it saw fit.<sup>101</sup>

### *Whitney Responds*

On February 13, four days after Senator Fletcher introduced the Securities Exchange Act, Richard Whitney announced three additions to the New York Stock Exchange's governing regulations. The first new rule disallowed NYSE members, or their affiliated companies, from engaging in any trading pools or other actions aimed at "unfairly influencing the market price of any security."<sup>102</sup> The second new regulation prohibited NYSE specialists, or their affiliated companies, from either granting or obtaining options relating to the securities in which they specialized. And the final new rule barred NYSE specialists from revealing any information about the orders with which they had been entrusted (certain NYSE committees were exempt from this final prohibition).<sup>103</sup>

In addition to announcing the new rules, Whitney gave his first interviews in over a year. He attacked a number of the "rigid and unworkable provisions" of the proposed Securities Exchange Act, claiming that the New York Stock Exchange had already adopted sufficient rules "to prevent excessive speculation."<sup>104</sup> In particular, he argued that the bill's high margin requirements "might force the liquidation of many accounts," that the bill's prohibition on lending against unlisted securities would "deprive people owning unlisted securities of the right to use them as the basis of credit in brokerage accounts," and that the bill's ban on exchange members acting as securities dealers would unduly harm the nation's smaller regional securities markets and would "destroy the odd-lot business which now affords the only market to investors holding less than one hundred shares of stock."<sup>105</sup> But Whitney reserved his harshest criticism for the publishing requirements of the bill:

Probably the worst features of the bill are those which purport to regulate corporations and corporate practices by imposing conditions upon the listing of securities upon exchanges. The bill requires every corporation listed on an exchange to register its securities with the Federal Trade Commission. The minimum requirements set forth in the bill are so burdensome that corporations may be unwilling to keep their securities listed on any exchange. Furthermore, the Federal Trade Commission is given unlimited power to require additional information in regard to corporate affairs which like all other reports or information furnished to the Commission, must be made available to the public. These powers are so extensive that the Federal Trade Commission might, in effect, control the management of every listed company.<sup>106</sup>

Additionally, Whitney stated that the potential dissemination of a company's "confidential statistics," which could result under the bill's publishing mandate, "would be destructive of American industry because it would furnish vital information to foreign competitors."<sup>107</sup>

Led by Whitney, the heads of the nation's stock exchanges and brokerages quickly began a wide-reaching campaign against the Securities Exchange Act, rallying their colleagues across the country via telegram and swamping congressmen with a flood of messages, phone calls, and letters aimed at

crushing support for the bill. Brokers argued that the act was far too harsh and restrictive and that it would likely drive "speculation and investing in American stocks to foreign markets" if enacted.<sup>108</sup>

On February 15, Whitney sent a copy of the bill and a letter criticizing it to all companies listed on the NYSE, claiming that the proposed legislation could end up "destroying the market for their securities."<sup>109</sup> On the same day, he also sent a copy of the bill and a different letter to every member of the exchange. The letters, which were printed in the following day's *Wall Street Journal*, highlighted specific facets of the proposed legislation that exchange members and listed firms would likely find disagreeable. In his letter to listed companies, for example, Whitney drew attention to provisions in the bill that would impose high fines on firms for noncompliance, would increase companies' vulnerability to lawsuits brought by investors, and would place securities trading limitations on directors, officers, and other large shareholders. In his letter to NYSE members, Whitney highlighted a number of other provisions, including those that would ban short selling, limit how much members could borrow, and grant the FTC the right to suspend or expel exchange members for perceived violations.<sup>110</sup>

The *New York Times* wrote that Whitney's response to the bill "was regarded in Wall Street as the broadest program of education on a Federal measure which the Exchange has ever directed toward the financial and business communities."<sup>111</sup> Senator Fletcher chose different words to describe the response:

The propaganda released by the Exchange officials is intended to persuade the people that regulation of that Exchange and the other Exchanges by the Federal Government will hurt business. Whose business? Only that of brokers who have lined their pockets by disregarding the interest of their customers.<sup>112</sup>

### *Pecora Attacks the NYSE*

In mid-February, while Whitney and others were attempting to discredit the newly introduced Securities Exchange bill, Pecora was busy revealing several instances in which the New York Stock Exchange had failed to prevent the manipulation of security prices. Specifically, the Banking Committee detailed trading pools in the stock of alcohol corporations that had occurred over the previous summer. The Committee presented an internal NYSE report which showed that the stock exchange had conducted its own examination of these suspect alcohol-stock transactions several months earlier. According to its report, the New York Stock Exchange had concluded that there had been "no material deliberate improprieties."<sup>113</sup> Pecora, however, showed that there had indeed been a concerted effort to artificially drive up the price of alcohol stocks and that those involved benefited considerably. Regarding the Banking Committee's findings, the chairman of the New York Stock Exchange's listing committee admitted to Pecora that "a cog slipped somewhere" and that his office was to blame for making a rare mistake.<sup>114</sup>

### *Whitney to Testify*

On February 22, 1934, Whitney was called to testify during the congressional hearings on the proposed Securities Exchange Act.<sup>115</sup> Whitney aimed to persuade lawmakers to strike down the bill, but he faced significant resistance. The Pecora hearings had impressed upon the nation a desire for financial reform, and the recent inquiry into the 1933 alcohol pools had just shown that Whitney's New York Stock Exchange had failed in one key area of self-regulation. However, in the two weeks since the bill was introduced, Whitney had effectively mobilized much of the financial world to oppose the act and to publicly denounce it as a heavy-handed overreaction. With these two opposing



forces at play, would Whitney be able to convince Congress that the Securities Exchange Act granted the FTC too much regulatory power and that it was in the nation's best interest to let stock exchanges police themselves? Or would Whitney's comments fall on deaf ears, with the legacy of the Pecora hearings helping to carry another sweeping financial reform bill through to law?

Exhibit 1 Dow Jones Industrial Average, January 1, 1920 to February 21, 1934



Source: Adapted from Dow Jones, "Dow Jones Index | Averages | Index Data," Dow Jones Indexes website, Dow Jones Averages, Historical Values, <http://www.djindexes.com/mdsidx/index.cfm?event=showavgIndexData>, accessed September 25, 2008.

## Exhibit 2 Securities Market Data, 1910-1933

	Dow Jones Industrial Index (year-end values)	Corporate Security Issues (\$ millions)		Sales on the New York Stock Exchange		Common Stock Price Indexes (1910=100)			
		Bonds and Notes	Common and Preferred Stocks	Volume of Stocks (millions)	Par Value of Bonds (\$ millions)	Railroads	Industrial	Utilities	Composite
1910	59.60	1,113	405	164	635	100.0	100.0	100.0	100.0
1911	59.84	1,387	352	127	890	101.0	97.4	103.6	100.6
1912	64.37	1,350	904	131	675	100.4	105.8	105.7	102.6
1913	57.71	1,194	452	83	502	87.5	91.2	92.9	89.3
1914	54.58	1,175	262	48	462	76.9	83.6	88.5	80.1
1915	99.15	1,111	325	173	961	91.9	136.3	105.5	105.8
1916	95.00	1,405	782	233	1,150	88.7	140.9	107.2	105.6
1917	74.38	1,076	455	186	1,057	68.4	105.8	77.2	78.5
1918	82.20	1,047	298	144	2,063	73.1	123.0	75.8	87.0
1919	107.23	1,122	1,546	317	3,809	66.4	161.1	69.7	99.1
1920	71.95	1,750	1,038	227	3,977	63.3	105.3	66.9	76.5
1921	81.10	1,994	275	173	3,324	64.5	113.1	79.0	80.1
1922	98.73	2,329	621	259	4,370	76.0	141.4	93.7	98.8
1923	95.52	2,430	736	236	2,790	71.6	140.3	94.2	95.8
1924	120.51	2,655	865	282	3,804	89.2	165.0	109.6	114.8
1925	156.66	2,975	1,247	454	3,384	102.9	209.1	128.4	139.9
1926	157.20	3,354	1,220	451	2,987	109.4	214.1	131.8	144.1
1927	202.40	4,769	1,738	577	3,269	129.0	278.8	162.7	183.6
1928	300.00	3,439	3,491	920	2,903	142.4	381.9	232.9	245.5
1929	248.48	2,620	6,757	1,125	2,982	137.9	299.5	265.9	211.4
1930	164.58	3,431	1,526	810	2,764	94.1	202.0	200.6	146.8
1931	77.90	2,028	343	577	3,051	32.3	106.0	115.8	75.6
1932	59.93	620	23	425	2,967	25.6	91.1	100.7	65.2
1933	99.90	227	152	655	3,369	41.8	162.8	87.0	97.7

Source: Adapted from Peter L. Rousseau, "Common stock prices: 1802-1999," and "Corporate security issues: 1910-1934," and "Sales of stocks and bonds on the New York Stock Exchange: 1879-1999," *Historical Statistics of the United States, Earliest Times to the Present: Millennial Edition*, eds. Susan B. Carter et al. (New York: Cambridge University Press, 2006), tables Cj800, Cj801, Cj802, Cj803, Cj834, Cj837, Cj857, Cj858; Dow Jones Industrials Average (Actual), Global Financial Data, Inc., accessed February 10, 2009.

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<sup>28</sup> Seligman, pp. 15-17.

<sup>29</sup> Seligman, p. 17; "Copper Profits of J.D. Ryan and Partners Bared," *Chicago Tribune*, June 5, 1932, p. 6.

<sup>30</sup> Seligman, pp. 17-18; "Copper Profits of J.D. Ryan and Partners Bared," p. 6; "Raskob Challenges Short Sales Charge at Senate Inquiry," *New York Times*, June 4, 1932, pp. 1, 16.

<sup>31</sup> "Wall St. Inquiry Suddenly is Ended," *New York Times*, June 25, 1932, p. 19.

<sup>32</sup> Seligman, pp. 18-20; "Senators to Sift Insull Collapse," *New York Times*, November 18, 1932, p. 27; "Stock Trade Probe Will Be Resumed," *Wall Street Journal*, November 18, 1932, p. 10; Arthur Krock, "Major Issues on Schedule," *New York Times*, December 5, 1932, p. 1.

<sup>33</sup> Seligman, p. 20; "I. B. Cooper Heads Market Inquiry," *New York Times*, January 11, 1933, p. 3.

<sup>34</sup> Quoted in "Cooper, Hampered, Quits Stock Inquiry," *New York Times*, January 18, 1933, p. 5.

<sup>35</sup> Quoted in "Pecora Appointed for Stock Inquiry," *New York Times*, January 25, 1933, p. 23.

<sup>36</sup> Quoted in "Pecora Appointed for Stock Inquiry," p. 23; Seligman, p. 21.

<sup>37</sup> Scott B. MacDonald and Jane E. Hughes, *Separating Fools from their Money: A History of American Financial Scandals* (New Brunswick, NJ: Transaction Publishers, 2007), pp. 103-108; Seligman, p. 21; Pecora, pp. 226-227.

<sup>38</sup> MacDonald and Hughes, pp. 111-113. Seligman, p. 22.

<sup>39</sup> Christopher J. Castaneda and Clarence M. Smith, *Gas Pipelines and the Emergence of America's Regulatory State: A History of Panhandle Eastern Corporation, 1928-1993* (Cambridge, UK: Cambridge University Press, 1996), p. 74.

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<sup>40</sup> Franklin D. Roosevelt, "Commonwealth Club Address," September 23, 1932, The New Deal: Franklin D. Roosevelt Speeches, Faculty Research, Pepperdine University School of Public Policy website, <http://publicpolicy.pepperdine.edu/faculty-research/new-deal/roosevelt-speeches/fr092332.htm>, accessed September 19, 2008.

<sup>41</sup> "Securities Given for Stock," *New York Times*, February 16, 1933, p. 8; "Insull Stock Deal Netted \$25,000,000," *New York Times*, February 16, 1933, p. 8; Seligman, p. 22.

<sup>42</sup> "Dawes Concedes Bank Abused Law in Insull Loans," *New York Times*, February 17, 1933, p. 1; "Insull Stock Deal Netted \$25,000,000," p. 8.

<sup>43</sup> Quoted in Pecora, pp. 225-228.

<sup>44</sup> Seligman, p. 23; "Dawes Concedes Bank Abused Law in Insull Loans," pp. 1, 12.

<sup>45</sup> Seligman, p. 23; "Dawes Concedes Bank Abused Law in Insull Loans," p. 12.

<sup>46</sup> Thomas F. Huertas and Joan L. Silverman, "Charles E. Mitchell: Scapegoat of the Crash?" *Business History Review* 60, no. 1 (Spring 1986): 82; "Mitchell Avoided Income Tax in 1929 by '2,800,000 Loss,'" *New York Times*, February 22, 1933, p. 1; Jerry W. Markham, *A Financial History of the United States* (Armonk, NY: M.E. Sharpe, 2002), p. 116; Seligman, pp. 23-24.

<sup>47</sup> "Mitchell Avoided Income Tax in 1929 by '2,800,000 Loss,'" p. 1.

<sup>48</sup> "Damnation of Mitchell," *Time*, March 6, 1933; United States BLS Consumer Price Index, Global Financial Data, Inc., accessed February 9, 2009; Huertas and Silverman: 82, 88-91.

<sup>49</sup> Pecora, p. 127.

<sup>50</sup> Pecora, pp. 127-128.

<sup>51</sup> Quoted in Pecora, p. 81.

<sup>52</sup> Quoted in Pecora, pp. 78-79; Seligman, p. 24.

<sup>53</sup> "Damnation of Mitchell"; Pecora, pp. 84-87, 111.

<sup>54</sup> Pecora, pp. 88-94; Seligman, pp. 24-25.

<sup>55</sup> "National City Sold Peru Bond Issues in 'Honest Mistake,'" *New York Times*, February 28, 1933, pp. 1, 6; Seligman, pp. 27-28; Pecora, pp. 96-104.

<sup>56</sup> Pecora, pp. 105-112; Markham, p. 117.

<sup>57</sup> Quoted in Pecora, p. 124.

<sup>58</sup> Pecora, pp. 125-126; "City Bank Officer Bares Ramsey Loan," *New York Times*, March 2, 1933, pp. 1, 9.

<sup>59</sup> M. R. Werner, *Privileged Characters* (New York: R. M. McBride & Company, 1935), pp. 467-469; Pecora, pp. 121-123; Peach, p. 133.

<sup>60</sup> Franklin D. Roosevelt, "Inaugural Address," March 4, 1933, The American Presidency Project website, <http://www.presidency.ucsb.edu/ws/index.php?pid=14473>, accessed May 2008; "Profit in Mergers Told to Senators," *New York Times*, March 3, 1933, p. 25.

<sup>61</sup> State banks were also inspected during the holiday, though these examinations were performed by state-level examiners. James S. Olson, *Historical Dictionary of the Great Depression, 1929-1940* (Westport, CT: Greenwood Press, 2001), p. 22.

<sup>62</sup> On January 21, 1932, the initial banking reform bill was presented to the Senate. This bill, which did not include a deposit insurance provision, resulted from more than a year's worth of investigation on the part of a Senate Banking and Currency Committee subgroup. The bill was withdrawn, revised, and reintroduced on

April 18, 1932. After passing the Senate, the bill died in the House, as the congressional session ended before the bill was brought to a vote. On the very first day of the special congressional session that Roosevelt called following his inauguration, the bill was again introduced. The bill was disregarded, however, as congress focused on the more pressing matter of the emergency bank holiday. Revised to include federal deposit insurance, the bill was again presented to the Senate on May 1, 1933. The revised senate bill, proposed by Carter Glass, was eventually merged with a very similar bill proposed by Representative Henry Steagall. Congress passed the resulting Glass-Steagall bill on June 13, 1933. For more, see Edwin Walter Kemmerer, *The ABC of the Federal Reserve System*, 10th ed. (Princeton, NJ: Princeton University Press, 1936), pp. 190-192; Marcus Nadler and Jules I. Bogen, *The Banking Crisis: The End of an Epoch* (New York: Dodd, Mead & Company, 1933), pp. 52-53.

<sup>63</sup> David A. Moss, *When All Else Fails: Government as the Ultimate Risk Manager* (Cambridge, MA: Harvard University Press, 2002), pp. 117-118.

<sup>64</sup> All member banks of the Federal Reserve System were required to join the deposit insurance system. Banks that were not part of the Federal Reserve System could become insured as well, on condition that they join the Federal Reserve System in the near future. All participant banks were required to contribute an amount equal to 0.25% of their deposits to the Temporary Deposit Insurance Fund, with another 0.25% being callable at the fund operators' discretion. This Temporary Deposit Insurance Fund backed each depositor up to \$2,500 starting on January 1, 1934. On July 1 of that year, the Federal Deposit Insurance Corporation (FDIC), which was to be initially capitalized by contributions from the 12 regional Federal Reserve Banks and the Treasury, was supposed to permanently replace the temporary fund. This did not happen, however, and the temporary fund was extended by a year and expanded to insure up to \$5,000 per depositor. In August of the following year, the Banking Act of 1935 replaced the temporary fund with the permanent FDIC and kept the insurance at the \$5,000 level. At this time, member banks' payments to the now permanent insurance fund were reduced to 0.083% of their deposits. For more, see Charles W. Calomiris and Eugene N. White, "The Origins of Federal Deposit Insurance," in *The Regulated Economy: A Historical Approach to Political Economy*, eds. Claudia Goldin and Gary D. Libecap (Chicago: University of Chicago Press, 1994), pp. 175-176.

<sup>65</sup> Emmanuel N. Roussakis, *Commercial Banking in an Era of Deregulation*, 3rd ed. (Westport, CT: Praeger Publishers, 1997), p. 34.

<sup>66</sup> "Drastic Changes in Bank Methods Expected Soon," *Chicago Daily Tribune*, June 18, 1933, p. A8; Pecora, pp. 284-286.

<sup>67</sup> Quoted in "Bankers Assail Glass-Steagall 'Reform' Bill," *Chicago Daily Tribune*, June 15, 1933, pp. 29-30; "Roosevelt Hails Goal," *New York Times*, June 17, 1933, p. 1.

<sup>68</sup> Franklin D. Roosevelt, "Message to Congress on Federal Supervision of Investment Securities," March 29, 1933, The American Presidency Project website, <http://www.presidency.ucsb.edu/ws/index.php?pid=14602&st=caveat+emtor&st1>, accessed May 2008; "President Takes Lead," *New York Times*, March 30, 1933, p. 1; Seligman, p. 75.

<sup>69</sup> Franklin D. Roosevelt, "Message to Congress on Federal Supervision of Investment Securities".

<sup>70</sup> Seligman, pp. 53-57, 63-70; Robert Sobel, *The Big Board: A History of the New York Stock Market* (Washington, DC: Beard Books, 2000), p. 294.

<sup>71</sup> "Truth in Securities' Bill Repassed by House, Senate," *Wall Street Journal*, May 25, 1933, p. 10.

<sup>72</sup> Seligman, pp. 48-49, 70-71.

<sup>73</sup> Franklin D. Roosevelt, "Excerpts from the Press Conference," March 29, 1933, The American Presidency Project website, <http://www.presidency.ucsb.edu/ws/index.php?pid=14604&st=&st1>, accessed September 19, 2008.

<sup>74</sup> Quoted in Seligman, pp. 75-76.

<sup>75</sup> Seligman, p. 76; "Stock Exchange Curbs Gambling; High Margins Set, Pools Checked," *New York Times*, August 3, 1933, p. 1.

<sup>76</sup> Seligman, pp. 71-72, 76-81.

<sup>77</sup> "J.P. Morgan Faces Questioning Today," *New York Times*, May 23, 1933, p. 27; "Now it is Told," *Time*, June 5, 1933; Seligman, pp. 31; Pecora, p. 4; Sobel, *The Big Board*, p. 294.

<sup>78</sup> Pecora, pp. 4-5; Seligman, pp. 31-32.

<sup>79</sup> "Rich Men Pay no Tax," *Washington Post*, May 24, 1933, p. 6; Seligman, p. 33.

<sup>80</sup> Seligman, pp. 34-35; Pecora, pp. 20-28.

<sup>81</sup> Pecora, pp. 28-34; Seligman, pp. 34-35; Sobel, *The Big Board*, pp. 238-239.

<sup>82</sup> Pecora, p. 5; Seligman, p. 37.

<sup>83</sup> "Why it Hurts," *New York Times*, May 27, 1933, p. 12.

<sup>84</sup> Seligman, p. 38; "Glass Bank Bill Passed by Senate," *New York Times*, May 26, 1933, p. 1; "Roosevelt Hails Goal," *New York Times*, June 17, 1933, p. 1.

<sup>85</sup> United States Senate, *Hearings Before the Committee on Banking and Currency, Part 2: (J. P. Morgan & Co.; O. P. Van Sweringen), May 26, 31, June 1, 2, 5, 6, 7, 8 and 9, 1933* (Washington, D.C.: United States Government Printing Office, 1934), pp. 307-956; United States Senate, *Hearings Before the Committee on Banking and Currency, Part 3: Kuhn Loeb; Pennroad Corporation, June 27, 28, 29, 30, and July 6, 1933* (Washington, D.C.: United States Government Printing Office, 1934), pp. 957-1533; United States Senate, *Hearings Before the Committee on Banking and Currency, Part 4: Dillon, Read & Co., October 3 to 13, 1933* (Washington, D.C.: United States Government Printing Office, 1934), pp. 1535-2277; United States Senate, *Hearings Before the Committee on Banking and Currency, Part 5: Chase Securities Corporation, October 17 to 25, 1933* (Washington, D.C.: United States Government Printing Office, 1934), pp. 2279-2741; "Damnation of Mitchell".

<sup>86</sup> Pecora, pp. 137-138.

<sup>87</sup> The price of Chase National stock just prior to the market crash of 1929 was actually \$283 per share. However, because the stock had recently undergone a 5-for-1 split, to accurately compare its value to 1927 prices, the 1929 share price had to be multiplied by five, thus resulting in the quoted value of \$1,415. Pecora, pp. 149-151, 184.

<sup>88</sup> Quoted in United States Senate, *Hearings Before the Committee on Banking and Currency, Part 6: Chase Securities Corporation (Continued), October 26 to November 10* (Washington, D.C.: United States Government Printing Office, 1934), pp. 2435-2436, 2835.

<sup>89</sup> Quoted in *Hearings Before the Committee on Banking and Currency, Part 6: Chase Securities Corporation, October 26 to November 10*, p. 2835.

<sup>90</sup> Pecora, pp. 142-146, 268-269.

<sup>91</sup> Pecora, pp. 147-158, 184, 200-201; "'Tax-Saving' Deals Related by Wiggin: He Paid \$4,624,905," *New York Times*, November 2, 1933, p. 1.

<sup>92</sup> Pecora, p. 161; Arthur E. Wilmarth, Jr., "Did Universal Banks Play a Significant Role in the U.S. Economy's Boom-and-Bust Cycle of 1921-33? A Preliminary Assessment," in *Current Developments in Monetary and Financial Law*, vol. 4, International Monetary Fund (Washington, DC: International Monetary Fund, 2005), p. 577.

<sup>93</sup> Quoted in "Aldrich Bans Chase Pools; Wiggin Bares Huge Profits," *Washington Post*, October 28, 1933, p. 1; "Chase Bank Drops Half of Its Board," *New York Times*, May 17, 1933, p. 23; Pecora, p. 140.

<sup>94</sup> "Aldrich Bans Chase Pools; Wiggin Bares Huge Profits," p. 1.

<sup>95</sup> Quoted in Seligman, pp. 82-84.



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<sup>96</sup> *Legislative History of the Securities Act of 1933 and Securities Exchange Act of 1934, Vol. 5*, compiled by J. S. Ellenberger and Ellen P. Mahar (South Hackensack, NJ: Fred B. Rothman & Co., 1973), Item no. 16, pp. V-20.

<sup>97</sup> *Legislative History of the Securities Act of 1933 and Securities Exchange Act of 1934, Vol. 5*, Item no. 16, pp. 4-20.

<sup>98</sup> Seligman, pp. 84-85; *Legislative History of the Securities Act of 1933 and Securities Exchange Act of 1934, Vol. 4*, Item no. 5, p. 2264.

<sup>99</sup> Quoted in *Legislative History of the Securities Act of 1933 and Securities Exchange Act of 1934, Vol. 4*, Item no. 5, p. 2264.

<sup>100</sup> *Legislative History of the Securities Act of 1933 and Securities Exchange Act of 1934, Vol. 4*, Item no. 5, pp. 2264-2272.

<sup>101</sup> *Legislative History of the Securities Act of 1933 and Securities Exchange Act of 1934, Vol. 4*, Item no. 5, pp. 2264-2272; Pecora, p. 269.

<sup>102</sup> Whitney quoted in "Three Tight Rules Added by Exchange," p. 29.

<sup>103</sup> "Three Tight Rules Added by Exchange," p. 29.

<sup>104</sup> Whitney quoted in "Whitney Fears Rigidity of Regulatory Bill Might Freeze Organized Regulatory Markets," *Wall Street Journal*, February 14, 1934, pp. 1, 9; "Three Tight Rules Added by Exchange," p. 29.

<sup>105</sup> Whitney quoted in "Whitney Fears Rigidity of Regulatory Bill Might Freeze Organized Regulatory Markets," p. 9.

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<sup>107</sup> Whitney quoted in "Whitney Fears Rigidity of Regulatory Bill Might Freeze Organized Regulatory Markets," p. 9.

<sup>108</sup> "Stock Market Bill Viewed as Faulty," *New York Times*, February 17, 1934, p. 21; Seligman, p. 89.

<sup>109</sup> "Whitney's Views on Trading Bill," *Wall Street Journal*, February 16, 1934, p. 7; "Whitney Extends Market Bill Fight," *New York Times*, February 16, 1934, p. 27.

<sup>110</sup> "Whitney's Views on Trading Bill," p. 7.

<sup>111</sup> "Whitney Extends Market Bill Fight," p. 27.

<sup>112</sup> Senator Fletcher quoted in "Fletcher's Statement on Stock 'Propaganda,'" *New York Times*, February 22, 1934, p. 2.

<sup>113</sup> Quoted in "Flexibility Urged in Exchange Bill," *New York Times*, February 15, 1934, p. 20; "Exchange 'Slipped' on Alcohol Issue," *New York Times*, February 17, 1934, p. 16; Pecora, pp. 272-282.

<sup>114</sup> "Exchange 'Slipped' on Alcohol Issue," p. 16; Pecora, pp. 272-282.

<sup>115</sup> "Whitney Testifies Today," p. 2; Seligman, p. 90.