

MEMORANDUM

DATE April 8, 1937

TO: James M. Landis, Chairman

FROM: Milton Katz

SUBJECT: Attached draft of letter re Konversionskasse 3% Dollar Bonds

Attached is a draft of a proposed letter to "The Economist", London, England, prepared by Francis T. Greene.

I should like to make the following suggestions:

(1) The second half of the letter, referring to so much of the dispatch in "The Economist" as relates to our comment concerning the possibilities of conflicting interest and preferential treatment for the bankers, should be omitted. On this subject, the comment in "The Economist" amounts to no more than an expression of an opinion by their Berlin correspondent concerning our action, and is hardly the sort of thing we ought to trouble to answer.

(2) In regard to the first point made by "The Economist", I think that Greene's draft, while in form somewhat too defensive, in substance contains the only possible answer. It seems to me, however, that "The Economist" would have a come-back. Our statement specifically says that the data concerning the unrecorded debt "came to the attention of the Securities and Exchange Commission" in November, 1936, after some six or seven weeks of an attempt on our part to get the German Government to make certain changes in the registration statement. There is very little doubt that this statement of ours can be so used as to make us look rather fatuous.

Since we obviously don't want to get into a running argument with "The Economist", and since we have no answer that would conclusively shut them up, I think we ought to drop the whole subject and refrain from sending any letter to them.



Enclosures

Milton Katz-kb

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON

OFFICE OF THE CHAIRMAN

Editor, "The Economist"
 8 Bouverie Street
 London, England

Dear Sir:

The March 20, 1937 issue of "The Economist" referring to the statement published by this Commission relative to the guaranteed 3% Dollar Bonds of the Konversionskasse für deutsche Auslandsschulden as recently offered in exchange for certain unpaid interest claims against German obligors has come to my attention. Inasmuch as the comment of your Berlin correspondent indicates possible misconception as to the registration of securities under the United States Securities Act of 1933, as amended, I am enclosing a copy of Release No. 1294 containing the text of the statement as released on the effective date of the registration of this issue of Funding Bonds and, in addition, I shall explain briefly the limited functions of the Commission in administering the registration requirements of this Act.

The Berlin despatch on page 642 of this issue criticizes the Securities and Exchange Commission for not having been familiar with the facts bearing on the so-called "secret debt" of the Reich prior to November of 1936. But the registration statements covering this issue of guaranteed bonds were not filed by the Conversion Office and the German Government until the latter end of September. As you are probably aware, the Securities Act of 1933 regulates the distribution of new security issues and, in substance, creates only a mechanism for achieving publicity of all the circumstances material to a considered appraisal of the securities registered. Under the Act a registration statement automatically becomes effective twenty days after the filing thereof or twenty days after the filing of the last amendment to the registration statement unless the Commission institutes formal action against the statement based on charges that it is false or misleading. The twenty days allowed

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for examination of registration statements is obviously so short a period of time as to preclude extended inquiry into all the extraneous factors, not disclosed in the registration statement, which may bear upon the accuracy or adequacy of the representations made in the many registration statements continuously being filed. Section 23 of the Securities Act of 1933 recognizes the impossibility of such examinations into the truth of all statements made by a registering issuer and specifically provides that neither the filing nor effectiveness of a registration statement shall constitute a finding by the Commission that the statement is true and accurate on its face or that it does not contain untrue or misleading statements of material fact. The Commission of course strives to make as thorough an inquiry as possible into all the circumstances referred to in registration statements. Yet it is not required to and in fact cannot, make the immediate investigation of extrinsic facts which the remarks of your Berlin correspondent seem to presuppose. You will thus appreciate that this Commission, by no means omniscient and without previous occasion to study the present internal economy of the German Government, was not remiss in failing to discover reliable evidence of the existence and character of the so-called "unrecorded" "future short term obligations" of the Reich at the very outset of its examination of the pending registration statements.

The Berlin despatch also reflects upon the suggestion in Release No. 1294 that many of the American banking houses which had originally distributed the defaulted issues of German obligations also held short term credits, some of which were subject to the so-called "standstill agreements" and had obtained better treatment of their claims than those of the bondholders who may have looked to such houses of issue for protection. The Commission of course recognized that the first standstill agreement was negotiated and concluded prior to the German Government's foreign exchange restrictions, preventing service of German funded indebtedness. However, the fact remains that after the discontinuance in June of 1933 of interest and similar payments on the funded indebtedness held in this country, many of the American banks and banking institutions successfully continued to press for at least partial payments in respect of the short term credits, and, subsequent to

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that time, did occupy a position preferential to that of the holders of the German bonds which those houses of issue had previously sold and distributed to the American public. Regardless of the precise point of time at which preferential treatment of short term credits commenced, the existence of this adverse interest on the part of the Special Agents acting for the Conversion Office in connection with the exchange offering seemed a material factor and was therefore pointed out.

I hope that this letter adequately explains the background of the public statement of the Securities and Exchange Commission relative to the registration of the Konversionskasse bonds and the reason why definite and authentic information as to the unrecorded short term internal obligations of the German Government was not obtained until the later stages of its examination of these registration statements.

Very truly yours,

James M. Landis
Chairman

Enclosure:
Release No. 1294