

(March 18, 1935)

## Blue Sky Laws and Their Administration

By J. M. GODFREY, ESQ., K.C.

PRESIDENT JAMES:—Mr. Godfrey, gentlemen, this, I think is a day that may be termed a very happy one in the history of the Canadian Club—and also a colorful day. Here we have, on one hand, blue sky laws and, on the other, something of a red letter day. Our speaker, Mr. J. M. Godfrey, K.C., is an original member of the Canadian Club. Every guest at the head table is also a chartered member of the Club—organized in November, 1897. The first dinner—the inaugural dinner—was held on the 26th of January, 1898. Our good friend, Colonel Cooper on my left, was first president. Weekly luncheons were instituted in February, 1898, and have been carried on continuously for the past thirty-seven years, there being breaks only during the Summer months. There were thirty-seven charter members of the Canadian Club of Toronto. Of these thirty-two are still living. Several of them have moved away and taken up permanent residence elsewhere. Of the remainder every one is present here today who was not prevented by business. There are two cases where business engagements could not be broken. On your behalf I am sure we extend to those charter members a most hearty welcome here today.

Though over thirty-seven years of age, the Toronto Club was not the first Canadian Club. To Hamilton belongs that honor. In the Winter of 1893, the Canadian Club of Hamilton was formed and W. Sanford Evans was the first president. Shortly after the formation of the Toronto Club, the idea soon spread—not only east and west but

also north and, after that, the development was rapid. Today there are Canadian Clubs, Men's Canadian Clubs, Women's Canadian Clubs and Young Men's Canadian Clubs and the Young Women's Business Canadian Club. Not only are Canadian Clubs scattered from coast to coast across Canada but there are several in the United States. Great Britain has also its Canadian Clubs and there are a few in the larger cities of South Africa and Australia.

Turning from these remarks on history, a word about our speaker. Mr. Godfrey has occupied his present position just a little over five months. Judging from what one has read and heard he has certainly made his presence felt at Queen's Park and in other parts of Ontario. I think I voice the sentiments of the great majority when I say "more power to you." An able lawyer familiar with the intricacies of finance and possessing a keen mind and, above all, a determination to do what he considers right are attributes that Mr. Godfrey brings to his new work. Gentlemen, I have much pleasure in asking Mr. Godfrey to address you on the subject, "Blue Sky Laws and Their Administration."

MR. GODFREY:—Mr. Chairman, gentlemen, I think on behalf of the old originals, we won't call them contemptibles, we should express our thanks to the committee of the Canadian Club for bringing about this happy re-union. I would enjoy it better if I did not have to make this speech. My first recollection of the Canadian Club was of a dinner at Webb's—over Webb's restaurant. It was in 1897. Mr. Sanford Evans was trying to put over the idea of a Canadian Club in Toronto. Mr. Evans was having what you may call pretty heavy going. The situation was pulled out of the fire for him by an extremely witty speech made by my friend Joe Clark who is still Joe Clark and a very original speech made by my friend Col. John A. Cooper who was then only Jack Cooper and, as a result when Col. Cooper sat down, Mr. Evans saw the psychological moment and promptly called for the formation of a Canadian Club. Now, in the early days there were some things that were slightly different from today. We did not have the apparatus which I have in front of

me now. That certainly is the most striking difference. But in these days we all sat around—probably fifteen members, sometimes as high as twenty-five and everybody talked. Now I want these old fellows to know that only members of superior intelligence are allowed to talk. Then there was another difference which, I think, is of deep economic significance. In these days we only paid 25 cents for our luncheon. Today we have to pay a dollar for more than we ought to eat. Then as now we had a depression. I think the depression was about as far advanced as our present depression. I think so, because during most of that depression I was one of the unemployed, and I remember just about this time I was thinking of undertaking matrimony and, as in those days \$1,000 was quite sufficient for a young lawyer to get married on, I must have been getting a little business at the time.

Thirty-seven years ago—that is a long time to look back. I was just looking round me and I have come to the conclusion that eating a luncheon here with a speech once a week must be a healthy occupation. Because surely these fellows are good-looking insurance risks.

You did not have in those days Blue Sky Laws or any securities commissioners. The reason was this: in the year 1898 gold production of the Province of Ontario was \$278,078. It was only when there was a tremendous increase in gold production that a securities commissioner was necessary. I was telling my friend, Mr. Eddie Odette, the other day my commission had a Biblical basis. I quoted from I. Timothy, vi, 10, "Love of money is the root of all evil." He replied that his had an earlier Biblical basis. His went back to the Old Testament, back to Proverbs xx, 1, "Wine is a mocker, strong drink is raging."

Now the securities commission type of legislation originated in Germany in 1884 and in France in 1893. In Germany it was established then that the entire amount of stock authorized must be subscribed in good faith. Under French and German law the company does not enjoy corporate power and cannot do business until the State is certain that fictitious or watered stock is not being used.

A special committee of the British Board of Trade in 1895 considered this type of legislation and rejected as futile and dangerous, every suggestion for a public inquiry by the Registrar or other official authority into the soundness, good faith and prospects of a proposed promotion.

I got a letter the other day from a friend of mine in Great Britain who is a well-known financier. He said that he thought that a securities commission was long overdue in Great Britain. However, that is for them to decide. Now this type of legislation did not originate in the United States, though the first Blue Sky Law was passed in Kansas in 1911. It was named "Blue Sky", some people say, because some promoters would sell lots in the blue sky; my own theory is that it comes from the good old poker game. "the sky is the limit"—especially when it comes to some of these high pressure fellows.

The Governor of Kansas, who was the proponent of this legislation, announced that its object was "the regulation and supervision of all kinds of companies in the same manner as our banks are now regulated and supervised." It was a tall order and attempted too much. The result was it had to be amended in 1913. That was rapidly followed by many other States and the reason was this. When the security act was passed the promoters and the high pressure fellows abandoned that State and went to States where they did not have a securities commission. The result was that one State after another in self-defence had to adopt the securities act and appoint a securities commissioner. As a consequence, ten years after the passing of the Kansas act there were securities acts in forty-three out of the forty-eight states, and now there is a Securities Act in every state of the union.

In 1929 there was a meeting of Blue Sky Law Commissioners held in St. Louis and a model act was adopted. As an illustration I would like to give you a brief summary. "The purpose of the securities law of Illinois is to prevent the sale and disposition of fraudulent securities and to protect the public from the dishonesty and irresponsibility of persons engaged in disposing of securities of uncertain value."

Now with classified types of securities, only the first two classifications are exempt from the operation of the act, such as government bonds and things of that kind. Others have to be registered before they can be sold. All salesmen, of course, must be registered. No license is issued to sell any particular issue. The security issuer is told verbally he may proceed to sell. This is done so that the salesman cannot say that the issue has government approval. It is an offence to sell a security which has not been registered.

There are two types of acts in the States. One is the Blue Sky type, which is something in the nature of birth control. That is, it looks into these securities before it allows them to be sold. There is another type of act called the Fraud Acts. They won't interfere unless fraud has been or is being committed. It is generally regarded from opinions which I have read that of the two types of acts the Blue Sky Act is the more effective.

I want to read a statement from the Attorney-General's Department of New York with regard to the Fraud Act. "I do not think the present Fraud Act will be a success, although I intend to enforce it as far as possible. Fictitious stock sales should be nipped in the bud. It is too late to do this under the present Fraud Act which covers fraud only, and does not reach or deal with incompetent management as does the Blue Sky legislation under a Commissioner with power to investigate. I believe in the ordinary type of Blue Sky legislation, that is, that full information should be obtained from the promoters or dealers before they are allowed to sell securities. I consider that a Securities Commissioner is the proper way to deal with the situation."

The first legislation of this type was introduced into Canada by the Hon. Charles A. Dunning, who was then Prime Minister of Saskatchewan. I think probably Mr. Dunning will get more *kudos* out of that act than out of this Union Government some people want him to form. This was followed by similar acts in Manitoba and Alberta. The Attorney-General, the Hon. I. B. Lucas, introduced the Securities Act in Ontario in 1919, but it was

withdrawn. In 1921 the Hon. W. E. Raney, Attorney-General for the Drury Government, instructed Mr. A. H. O'Brien to prepare a report on Blue Sky legislation and that is one of the most comprehensive studies of Blue Sky legislation which I have come across.

After a few months experience in administering the Act I read Mr. O'Brien's report a few days ago. It was remarkable how well he had foreseen the necessities and the type of the administration which, in my judgment, should be given to this Act. There was no Act passed until 1930 when the present Securities Act was drawn and passed. Its authorship must be attributed to Mr. Arthur Rogers, now secretary of the Canadian Bankers' Association, and W. R. Cottingham, Manitoba Commissioner. In 1931 it was taken out of the hands of the Attorney-General and an independent Commissioner was appointed. That impersonal thing called a Commission! I understand that such a Commission may be subject, on occasions, to disembodiment. I am not referring to the past, just the future. Now it is a good Act. It had all the experience of the past and could incorporate the experience of the past. It is flexible and constitutional difficulties, so far as the Dominion companies were concerned, were gone around by putting in the Commissioner's hands power of licensing salesmen, security issuers and brokers. By that power you can practically control the situation. You can administer the Act either as a Fraud Act or as a Blue Sky Act. I have chosen to administer it as a Blue Sky Act. The powers which it confers upon the Commissioner are these. He can say who shall or shall not sell securities. He can say what securities can be sold, and on any occasion, if he suspects fraud, he can bring anyone before him for investigation, either publicly or privately and he has another power which is a big thing. He can, by simply telephoning a bank or trust company, tie up a bank account or securities of any person being investigated. So if I hear of any of you fellows not behaving, look out for your bank account. There is a lot of power there. There is no appeal from it, so I noticed in a discussion in the legislature. Gentlemen, there is an appeal from any decis-

ion of the Securities Commissioner. Whatever else you may say about this government up here it is democratic and all these Commissions have to be administered in a democratic way. The appeal may not be by court or a judge who, after all, is not specially qualified to pass judgments on the administration of this Act, but the appeal is to public opinion and that is what controls the administration of this department.

Now we do not require, under the Act, the registration of securities, but under regulation, we do require certain securities to be registered where they have been issued for considerations other than cash. But there are two exceptions to that. One is that it does not apply to issues by the Investment Dealers' Association. The other is, it does not apply to sales made by members of the Toronto Stock Exchange. Now, gentlemen, I think we have just about decided to bring all these issues in under the Act. I have come to the conclusion that they all require looking over just as well as mining issues. With regard to the Stock Exchange that has been fixed by requiring all new listings to be approved by the Commission. And that is working out in a very satisfactory way. Now that gives you some idea of the history of the thing. I have taken a good deal of time to tell you of a few things we tried to do.

When I went into this job I found a well-organized department running smoothly as to administration routine. There is an excellent registrar in W. A. O'Brien and I could practically forget the details and had time to think out and work out questions of general policy.

It was natural to do the obvious thing first. The city was simply infested with crooks and racketeers from the other side. As you know, they have a new Federal Exchange Commission over there and their activities had driven these gentlemen into Ontario, attracted by this boom in gold stocks. Well, one thing that was necessary was a strong investigation department. I frankly criticized the organization of the department as I found it because they had really no investigation department at all. There was only one investigator available. Well, I had to create an

investigation department and that cost money. You know what an obsession for economy this new government had. I wish some other people not so far away were afflicted with the same obsession. I made up my mind we had to have it, but how were we going to get the money? By the simple process of asking the brokers and salesmen to pay—by increasing their fees very substantially. I think I can say that whereas there was a deficit of \$14,000 last year there is going to be no deficit this year. Having got the money we are organizing our investigating department. The department was placed in charge of a very energetic gentleman, Col. D. F. Pidgeon.

The first thing, standing out like a sore thumb, were the boiler rooms, armed with a great battery of telephones—sometimes 25 and as high as 50, operated by well-trained salesmen called dynamos. These people had simply taken millions of money out of the people of this Province. I could tell you a most interesting story but time does not permit. We passed a regulation prohibiting selling by telephones to private residents and we did something else; we assumed that every man who ran a boiler room was financially undesirable. So we went to the Bell Telephone Company and after a little pressure, which I can put on by reason of this power of investigation, we got a complete record of the telephone and the statement of the long distance calls of every broker in Toronto. One boiler room had spent \$16,000 for August and September. We found a remarkable situation there. They were selling worthless vendor shares which cost them \$400, which they sold for something like \$600,000. Of that amount taken out of the public we have recovered \$192,000 in the past five and a half months. We closed them up and cleaned up that situation.

The result is about two months ago at a large hotel (I am not going to say what hotel), there were 96 of these gentlemen registered. The last I heard there were only five. The reason is because they dare not go back to the States. We have closed up about forty of these people and I think there are about 200 of their salesmen gone to parts unknown.

Now we also brought in the crown attorneys on the suggestion of the Attorney-General. We issued a warning to investors that was published in all the newspapers of the Province. It certainly pays to advertise. We increased our business by about four hundred per cent. We got results. We have handled hundreds of investigations, I do not know how many, and we have got some very good results out of them. The week before last we recovered \$25,340. Not bad in one week. Here are our totals as supplied by the auditor. In five and a half months we recovered for investors and shareholders, money taken away by fraud, \$192,703.45. Another thing, it did not cost the Province a cent because the brokers and salesmen paid for that. And you ask me is it fair to ask the brokers and salesmen to pay all this money to get this back for the people of the Province? Why certainly it is. They ought to pay for cleaning their own house. Furthermore when we got rid of all the financial undesirables, business will be left in the hands of reasonably honest people. They will have that business.

Now there is a constructive side to this whole question and I would like if I had the time to tell you some of the things we are doing. We are always running into companies that need re-organizing. For instance, the director of one company, which was being re-organized, came to me and he had a proposition for re-organization if he could put over what he wanted. He wanted to bring in \$300,000 capital to develop this market. His proposal was fair to the present shareholders but he had \$54,000 due to creditors. I said, "I approve of your plan and I am going to help you put it over." I wrote a letter. I was not worrying about the creditors. The shareholders wrote him a letter. He sent my letter to the creditors and I knew what would happen. The creditors telephoned me, and I advised them to accept that proposition. The result was we kept that mine going, \$20,000 a month is being spent, and it has the possibilities of becoming another good property with increased employment. After all, gentlemen, this unemployment question is the biggest thing we have to contend with. Just at present when peo-

ple are saying nice things I am going to take it all. We like a little word of praise. Here is a letter we received from one mining company. "We enclose a copy of the contract mentioned, and think you will agree that they have been very generous in protective clauses for our shareholders. It is hard for the writer to express appreciation of your assistance in the trying days that led up to the consummation of this deal, and it is no idle statement to say that without your interest and backing neither the compromise nor arrangements with the bank could have been consummated and the shareholders of this company have you to thank for their present position which, we believe, holds great promise for them." That is the sort of thing we appreciate. I could go on with several other cases. I am going to make an announcement in a day or so. We have taken a company out of bankruptcy and succeeded in getting a substantial number of shares in a new company for the old shareholders. I would like to say something about Mr. Peter Walls, mining engineer, who also has to do with that. That will be set forth in the public report. I hope to get something started which would mean \$450,000 expenditure in this Province and the opening up of a mine to get \$4,000,000 of ore, which means employment for 250 people.

I would like to say this in conclusion. We are one department that frankly looks after the capitalists. We represent capital. I do not agree that the capitalist system is doomed. Nowadays in the newspapers the capitalist system is alluded to and talked about. Some young people passed a resolution the other day saying the capitalist system is doomed. There is a friend of mine who made a speech the other day in which he said to bolster up the capitalist system it would be necessary to have a Fascist Military Dictator. Well, if either of these things happen I am through with my job, because if the capitalist system is doomed as it is in Russia there won't be any need for a Securities Commissioner, brokers or salesmen. I suppose the dictator himself will look after the capitalist. You have heard a good deal about a new deal. There is nothing so high sounding as that. What we try to do is

this—just to the best of our ability we try to give a square deal.

PRESIDENT JAMES:—Gentlemen, I am now going to call on Col. John A. Cooper, first president of the Toronto Canadian Club who will give you a few words and include an expression of thanks to the speaker.

EX-PRESIDENT COOPER:—Mr. President, Mr. Godfrey and gentlemen, I do not know that I have any message to bring to you except that I would advise any of you who desire to achieve fame to start early in life and do not leave it too late. Canada at the time when the Canadian Clubs were founded, as Mr. Godfrey has said, was passing through rather strenuous days and we felt that the young men of Toronto should have an organization which would perhaps create a little more hope and a little more optimism in their minds. That, I think, was the impelling influence which brought us together. So far as my part as first president of the Canadian Club was concerned, it was purely accidental. I had recently become editor of *The Canadian Magazine* which was rather a high-class publication. Therefore, I must be a rather high-class person. I had not been long enough on the job to be found out. Sanford Evans had the original idea. When he came from New York and suggested it, I naturally said I would be very glad to help him and along with a good many others we started in under Sanford to put over this idea, in which we were all interested. In a little room in Mason and Risch's warehouse on King Street we met one night and we formed the Club. There were preliminary meetings before that. Twenty-three gentlemen signed the role—I say gentlemen because I think they are all gentlemen. Most of them have proved that since. I said, "Sanford you sign first." He said, "No, John we are going to make you president, you sign. You have been longer in Toronto and know more of the men." Thus I became president. Next to having ability, it is well to have friends. My friend Mr. Williams down here wrote an article in my favorite journal and also the favorite journal of Mr. Godfrey—*The Mail and Empire*—and he tells the history of the Canadian Club there. It was suggested that

there be some speaker; and that is how the luncheon idea started. I could give you a nice story which reflected more upon myself than some of the rest of us. One day I thought I would invite the members of the executive to a luncheon which cost 25 cents per head and there were twelve or thirteen present. That was the first luncheon. Somebody suggested that another luncheon meeting be held in a week provided the president paid. So I accepted the challenge. I called a meeting in a couple of weeks and they came and they did not call on me to pay for the luncheon on that occasion. We got to the place where the executive and members were getting together for luncheon parties. There would be about twenty to thirty. As Mr. Godfrey pointed out, it was not with the idea of a listening club such as we have nowadays but a discussion club. But we got away from that idea at a later date. I think, as Mr. Williams points out, the Canadian Club of Toronto was the first luncheon club in North America.

The membership grew very rapidly. Some figures might be of interest just to show how quickly we grew. We had 57 members the first year and then by reference to the treasurer's accounts I found that 51 paid their fees. In the second year, under Mr. Sanford Evans the membership grew to 140. In the third year, under Mr. Wilkie it grew to 190. In the fourth year under Mr. Rundle it grew to 210. In the fifth year it grew to 450 and in the following year it touched 800. The following year, 1903-4, it passed the 1,000 mark.

I have in my hand here the report of 1903-4, with the list of the 1,000 members and the history of the Club. I do not know if there are any others in existence but any facts I give you are taken from this report. I also have here—I am just trying to make you jealous—but on account of the carefulness of my wife, I have the first annual report signed by myself.

This is what I know about the founding. We were enthusiastic about Canada and were concerned about the young men of Canada. We did not want to see them going to the United States which was a common habit between 1886 and 1896. We thought we would try and

make them more enthusiastic about Canada, and if we have succeeded that is our contribution. I thank you, gentlemen; now a word about Mr. Godfrey. In 1891 I was a member of a team of two men who were appointed by the University of Toronto to carry the annual debate to Queen's University. J. M. Godfrey was senior member of the team. I think I had more admiration for him after that evening was over than I have ever had since. He made what was called "a damned good speech." He won the debate. I have known him ever since. I felt that when he was put on this new job by a government, with which I have not a great deal of sympathy but for which I may have admiration later on, I felt he would do a very good job. I believe, in the minds of the business men of Toronto, he is honestly trying to do his job.

Because he is a charter member of this Club, because we have known him so long and favorably and because of his good work, I am sure we are all pleased to tender our sincere thanks for his coming here today and giving us, not so much the facts, but the atmosphere of the work which he is doing.