

Ethics in the Securities Business

In the securities industry, where transactions are dependent upon a trust relationship between a firm and its clients, few firms can boast that they have as high a standard of ethics or as strong a record of ethical conduct as Wayne Hummer and Company. The article which follows describes the origin of this unique firm and suggests the lessons to be learned from this instructive episode in American business history.

Wayne Hummer's Youth

Wayne Hummer was born in LaSalle, Illinois on August 24, 1884, the son of William B. and Tillie Nafziger Hummer. The father was a third generation American who had moved to LaSalle as a young man. There he secured a job as a clerk at a local drug store and subsequently acquired his own pharmacy. Once established as a business owner, William organized a commercial bank and became its president. It was an unspoken understanding in the Hummer family that young Wayne would eventually go to work for his father at the bank.

Wayne grew up in an atmosphere of respect for principle and excellence. His father was a stern man with a well-earned reputation for conducting business and personal affairs on a high ethical plane. The community was blessed by the presence of other high-minded business leaders, including F. W. Matthiessen, founder of the Western Clock Co. (Westclox), who donated a high school to LaSalle and personally selected a principal who was then instructed to make the high school one of the best in the country. The principal was an impressive Princeton graduate named Thomas J. McCormack, a classmate of Woodrow Wilson.

When the time came for Wayne Hummer to choose a college, he and his father consulted Principal McCormack who recommended Princeton. Young Hummer accepted the advice and entered Princeton as a freshman in 1903. A year later he transferred to the Wharton School of Finance, then the undergraduate business school at the University of Pennsylvania. In 1907, Wayne graduated from Wharton as president of his class.

As class president, Wayne invited Stuyvesant Fish, a prominent New York financier, to address the graduating class. Mr. Fish's message dealt with the idea that confidence is the cornerstone of all financial activity. [1] This idea greatly impressed Wayne and became a guiding principle during his business career.

The Apprenticeship

Upon graduation from Wharton, Wayne returned to his home in LaSalle. If Wayne had an uncertainty about his career plans this was dispelled within less than a week when his father told him to "...be down at the bank bright and early the next day." [2] This was not an unexpected message. As Wayne put it many years later: "In those days parents didn't ask their sons what they were going to do – they told them." [3]

There followed an 8-year apprenticeship in the banking business. In those days commercial banks existed mainly to serve the business community. While banks did accept both consumer and business deposits, their main activity was directed towards meeting the needs of their commercial customers. In accepting deposits and making loans, Wayne's father told him to "...always remember that this money belongs to the depositors and to be very careful about who we lend it to and to be sure that we get it back." [4]

Wayne's father died in November, 1907, before the young Wharton graduate had completed his first year at the bank. Because of Wayne's youth and inexperience, it was decided that Edward Wilson would serve as president of the bank until Wayne was ready. Eight years later, in 1915, Wilson decided it was time for Wayne to assume command. On a day in January, Wilson walked into Wayne Hummer's office and said, "It's time for you to take over as president of the bank. I'll become vice president." [5]

That "rite of passage" triggered a second hallmark event in Wayne Hummer's life. Earlier he had met and fallen in love with Anne McNally, daughter of a Chillicothe, Missouri bank president. The couple had not rushed into marriage, preferring instead to wait until Wayne assumed the presidency of the LaSalle bank. Once that occurred, the young couple made plans for the marriage which took place on June 12, 1916.

Wayne and Anne would later have a daughter, Barbara (born September 14, 1921) and two sons, William (born August 4, 1924) and Philip (born June 6, 1931). The boys would eventually follow their father in the banking and brokerage businesses.

Wayne Hummer -- Small Town Banker

Young Hummer lost no time in putting his mark on bank affairs. Shortly after assuming the presidency he traveled to New York on what he apparently regarded as an information-gathering trip. There he visited with prominent big city bankers, seeking ideas which he could use back in LaSalle. One idea which appealed to him was a newsletter which the National City Bank of New York published. Wayne quickly saw the value of such a publication in attracting new customers. Upon returning to LaSalle he initiated a newsletter of his own. It focused on news of the economy and on financial developments. And, in the "soft sell" manner which appealed to Wayne, it provided a vehicle which was expected to attract new customers. [6] Wayne personally wrote the letter, thereby forcing himself to keep abreast of developments at both the national and state levels.

Free banking existed during the latter half of the 19th century and through World War I. The Comptroller of the Currency and most state banking authorities were allowed to issue charters to those individuals who met very general and often loose banking requirements. Under this lax policy the number of banks grew to more than 29,000 by 1920.

While the number of banks was increasing markedly, many banks were facing adverse economic conditions in the 1920s. Shifts in the location of many business firms, deflation in the early twenties and the plight of the agricultural sector helped to cause the failure of over 5,000 banks during the decade.

Even though banks, particularly small town banks, were failing rapidly, the LaSalle National Bank prospered under Wayne's leadership. Throughout this period, and his entire banking career, Wayne remembered and applied his father's philosophy of protecting depositor's funds through making only sound loans and financial investments. The results justified Wayne's faith. The bank flourished in the twenties, and it prospered during the depression era when more than 9,000 banks (with deposits of \$7 billion) were forced to close their doors. It has continued to prosper to the present under the leadership first of Wayne and more recently of his son William.

While Wayne was protecting the financial integrity of the bank, he was also acting as a LaSalle community leader on a scale which still serves as a standard against which future community bankers must measure themselves. His early community leadership took two forms – branching into new business ventures and civic causes. In the business arena, Wayne took over his father's insurance agency at the time of the elder Hummer's death. Then in 1916, he bought a struggling furniture store and founded the Hummer Furniture Company. The original owners of the store had run into financial difficulties. Wayne restored the business to profitability. Creditors and employees benefited from the continued operation of the store and Wayne enriched his daily routine with the job of overseeing his investment in the new business.

The next business was a radio station which Wayne Hummer established in 1927. That was a period of time when radio was new and nobody could be sure that it would be a profitable business. But communities that had radio stations stood out as a progressive places to live and work, and community leaders throughout the country had to face up to the fact that a radio station was needed if for no other reason than local pride. It was with those thoughts in mind that Wayne Hummer took the gamble and set up a radio station on the second story of the furniture store. As William Hummer put it, "The radio station was both a community service and an investment. But the service element was the major motivation. In those days the return on investment in small town radio stations wasn't particularly good." [7]

Next Wayne invested in a hotel. He and other community leaders felt that a hotel was needed not only to accommodate travelers, but also to provide meeting facilities.

Finally, Wayne was an active member of the investor group which established the LaSalle-Peru Airways Company in 1929. They bought several airplanes, built a hanger just north of LaSalle, and established scheduled air service to Chicago.

Wayne's numerous business ventures eventually led him into civic activities. There was a tradition here. His father had been a leader of a group pushing for navigation improvements on the nearby Illinois River. Wayne became an active member of the LaSalle Chamber of Commerce in 1915. In 1928 he was elected president of the organization. By that time he had also become active in the Illinois State Chamber of Commerce and in 1930, that organization elected him its president. One of Wayne's proudest activities as a chamber leader was his push for better roads for LaSalle County. Years of dogged effort paid off in the early 1920s when the state legislature authorized highway improvements in the county.

In addition to his Chamber duties, he was very active in the Illinois Bankers Association. In recognition of his many contributions to the banking community, he was elected the association's youngest president in 1924.

Wayne was also an active member of the Republican Party. As a result, in 1932 he was appointed director of the Reconstruction Finance Corporation in Illinois. This federal government agency was a depression era attempt to make loans available to small businesses in danger of failing. Wayne served in this job until the Democrats came to power in 1933.

The Brokerage Firm

One of Wayne Hummer's weekly routines in LaSalle was to go to the bank to work on Sunday. His close friend and the bank's trust officer, George Barnes, would always be there to work with him and the two men would occasionally discuss a problem facing most small banks in those days – the problem of ethics in the bond brokerage industry.

The problem arose because representatives from Chicago and New York investment companies would call on the small town banks for the purpose of selling them securities. These salesmen did not act only as a broker agent when giving investment advice and executing orders for the banks, but would often be involved in the actual underwriting of the securities they were selling. Therefore, there was a potential for a serious conflict of interest when a salesperson gave advice on securities that his firm had purchased for resale.

During the 1920s numerous small-town banks and individuals relied on investment advice from these investment company representatives. The result was that many of these investors made unwise, and sometimes disastrous, decisions when buying securities from these companies.

Wayne Hummer avoided the problem by refusing to deal with the salesmen. He bought his own bonds and even began to help other bankers make wise choices. However, the ethics of the bond salesmen bothered him and the Sunday conversations with Barnes began to nurture a dream of some day starting a brokerage firm to give small town bankers a more ethical standard of service. The appeal in doing so was the opportunity to right a wrong. As Barnes recently put it, "We were furious. It just wasn't right!"^[8] That motivation is an important part of the story for it illustrates the fact that some entrepreneurs are driven by altruistic motives.

An Unexpected Opportunity to Start

In spring of 1929, Wayne was presented with an unexpected opportunity to implement his dream of starting a unique brokerage firm. He and George Barnes were playing golf at the Deer Park Country Club. It was an Illinois Bankers Association event. In the foursome were a securities broker, A.C. Baur, and Harvey Hill, an entrepreneur who was then president of the expanding Chicago Stock Exchange. At one crucial point in the game Hill turned to Baur and tried to sell him a membership in the stock exchange. Baur showed some interest but said he didn't have the needed funds to make the investment. Wayne Hummer jumped into the conversation with an offer to provide the money if Baur would represent a new brokerage firm which Hummer and Barnes wanted to start. Baur agreed.

In February, 1931, Wayne Hummer and George Barnes started their Chicago-based brokerage firm with funds borrowed by Wayne from the LaSalle National Bank. The firm was originally titled A.C. Baur, but was very shortly changed to Wayne Hummer and Company. The firm opened for business on February 16, 1931 in the Chicago Stock Exchange building. In 1932, the offices were moved to the Bankers' Building at 105

West Adams, a location that they occupied until 1977 when they moved to their present facilities at 175 West Jackson Boulevard.

Trying to start a new business, particularly a brokerage firm, following the 1929 Stock Market Crash as a major challenge. Add to this the fact that the new firm was to specialize in selling securities to small and medium size banks, at a time when thousands of banks were closing each year, and you had an almost impossible undertaking.

Commenting on these early days of the firm, Wayne stated in 1976, "The time [1931] couldn't have been worse. I don't know how we survived. But we were young and full of pep and I don't think there was a month that we lost money."

"Full of pep" they were. They immediately started their Bank Bond Comment Letter. This letter, which reviewed trends in the financial markets and suggested portfolio policy, was mailed directly to commercial banks. In 1932, when Harry A. Baum joined the firm, they started their Stock Market Comment Letter. With these two letters, plus personal correspondence sent to commercial bankers, the firm became a pioneer in direct-mail marketing. Today, these two letters reach over sixty thousand individuals and financial institutions.

In addition to using the mails to carry the firm's message, Wayne personally called on bankers in Iowa, Illinois, Indiana, Wisconsin, and Michigan. Quite often Wayne took his wife and two sons (Philip and William) with him as he traveled the Midwest. Recalling these early days, Philip stated that they were a trying period in their lives. "There was never time for lunch. The banks were open from 9:00 a.m. to 2:00 p.m. About the best we could hope for would be a candy bar to tide us over until the banks closed and the bank presidents could take time to hear what our father had to say." [10]

When the banks were closed for business, Wayne had a "fool-proof" method of attracting attention and getting into the bank to deliver his message. "He'd use a key to rap on the glass in the door of the bank. In those days, that's how the bank examiners got inside after hours. So the banker would come over and see who was coming around." [11]

While the firm did get on its feet during the early '30s, it required cost conscious measures and sacrifice on everyone's part. For example, the firm's staff would often be paid for three weeks after having worked a full month. As colorfully put by Harry A. Baum, "...employees did receive 'Hoover' vacations once a month – one week out of every four off without pay." [12]

Another Problem Emerges

The initial purchase of a seat on the Chicago Stock Exchange (which eventually became the Midwest Stock Exchange through mergers in 1949) limited the number of securities in which Hummer could deal. Consequently, Barnes was asked to purchase access to other exchanges. Memberships were quickly acquired in the Chicago Curb, the Chicago Board of Trade and New York Stock Exchange. In New York, Hummer brought in Walter Douglas who had a membership in the New York Stock Exchange. (His capital contribution to Wayne Hummer and Company was the market value of his seat on the New York Stock Exchange.)

At the New York Stock Exchange, Wayne Hummer discovered another ethical problem which he and Barnes proceeded to correct. The problem was that Hummer didn't have an office in New York and wasn't allowed to clear trades by mail. As a result the company had to give up 30 to 40 percent of the commission to have trades cleared. Barnes and Hummer filed what they called "a friendly suit" to have the courts declare the refusal to deal by mail an illegal restrictive practice. "It was a long battle, but a good battle," as Barnes was to say many years later. [13] When it was over, Hummer had won the right for his firm and others to clear by mail and earn the extra 30 to 40 percent of the commissions.

The Firm's Mission

The new brokerage firm was to have a unique mission of service to small town bankers and the general public. It would buy and sell securities for them without engaging in several practices which Wayne Hummer

regarded as unethical. In particular, Wayne Hummer and Company would:

1. Refuse to engage in the underwriting of new issues of securities;
2. Refuse to inventory stocks and bonds for resale; and
3. Refuse to encourage active trading in securities, but instead would foster a "buy and hold" investment strategy in the nation's strongest companies.

Click here to read other key principles and the firm's code of conduct are listed at the end of this article. These practices, which Hummer considered unethical, were almost universal in the securities industry, then and now. They were accepted by customer and broker alike. From the broker's standpoint, these practices could be the source of substantial earnings. As Barnes once put it, "Most firms would feel unfairly denied legitimate income if limited only to the agency business as we practiced it at Wayne Hummer and Company." [14]

But, in an impressive act of self-denial, Wayne Hummer refused to engage in these activities, all of which he regarded as unethical. Of course, to Wayne the extra income was of no consequence. What was important was to right a wrong. For a man whose life was dedicated to service above self this was not actually an act of self-denial, but rather an act of self-affirmation.

Growth Constrained by Mission and Lifestyle Marketing the Firm's Services

Wayne used a low-pressure approach to signing up new customers for the firm. Wayne's goal in the marketing effort was to make the public aware of the firm's existence and the fact that it was unique in acting strictly as a broker-agent for its customers. Wayne's sons, William and Philip, recall their father would often point out, "We have nothing to sell except service." [15]

Since the firm had a state policy against active solicitation of business, it offered a number of special services to attract customers. It published its free market letters (Bank Bond Comment Letter and the Stock Market Comment Letter), offered toll-free numbers to present and potential customers, provided portfolio evaluation and analysis, supplied (on a cost basis) securities record-keeping books and handled, without charge, estate valuations and transfers of securities for lawyers and bankers located in smaller communities.

A great deal of business was generated by banks which referred their depositors and customers to Wayne Hummer and Company, and by similar referrals from the firm's existing customers. Sometimes the referrals would take a surprising form.

As reported by Chicago Sun Times reporter Jerome Idaszak, "Harry A. Baum recalled spending 45 minutes with a woman who walked in, said she was caring for her aged mother and wanted to put a small savings into a stock. He sold her 10 shares of Commonwealth Edison."

"Weeks later, a man walked in, asked for Baum and handed him a check for \$350,000 and told Baum to invest it in what Baum chose. The man was the brother of the woman, had just sold his business and told Baum, 'Anyone who'd spend 45 minutes talking to my sister to sell her 10 shares of stock is the man who gets my business.'" [16]

Containing Costs While Enhancing Service

Since its inception in 1931 to the present, Wayne Hummer and Company has experienced an unbroken record of profits. A critical factor behind this accomplishment has been its ability to keep a close control over expenses, while giving excellent service to its customers.

To help contain costs the firm purposely stayed small. As late as 1989, Wayne Hummer and Company had only 150 employees between its Chicago office and its branches in Appleton, Wisconsin, and Aurora, Illinois. The small size supported a conservative ethos which included policies to (1) not employ outside salesmen, (2) not pay club dues or entertainment expense of the partners, (3) not allow expense accounts, and (4) not provide plush offices.

To enhance service to their customers, Hummer and Company has preferred to modernize their operations rather than open new offices. In 1962, they were the first firm to join the Midwest Stock Exchange computer accounting system. To speed up the execution of orders they installed a direct wire to the floor of the New York Stock Exchange in 1962. In 1977, the firm moved into its present offices on Jackson Boulevard. They equipped those facilities with the state-of-the-art electronic technology to give the best and fastest possible service to their customers.

Fostering Industry Change

In the best of all possible worlds it would be recorded that Wayne Hummer's example fostered a widespread improvement of ethical practice in the securities industry. Such, unfortunately, was not the case. Wayne Hummer and Company has remained unique in its determination to place principle above profit.

But, on several occasions Wayne Hummer and Company was able to exert leadership in achieving desirable changes in the industry. In the early 1940s, George Barnes developed a commission table based on "money involved" rather than on the number of shares. This new approach was quickly adopted by all the stock exchanges and the over-the-counter security dealers. During the same period, Barnes was also instrumental in the establishment of the Association of Stock Exchange Firms.

In 1962, the firm was in the forefront in stopping federal legislation that would have placed a 20% withholding tax on both interest and dividends. In the latter half of the 1970s, they were a leader in waging a fight against the capital gains tax on inherited property. This was a long battle, but a successful one, and such a tax was never enacted.

Collegial Management

To facilitate its commitment to higher principles, Wayne Hummer and Company was, and continues to be, a privately owned firm that has deliberately avoided merging with another company. This approach has allowed for the continuity and stability of the firm and the adherence to the policies instituted by Wayne Hummer in 1931.

Presently, Hummer and Company has 16 partners who have invested their own funds in the firm and share in its day-to-day management. These individuals were attracted to the firm because of both the principles established by its founder and the opportunity offered them to grow and prosper along with Hummer and Company.

In an interview conducted with Philip and William Hummer at the time their father was inducted into the Hall of Fame, Philip had the following to say:

"We've seen a lot of companies, especially service companies like you find in the securities industry, dominated by strong individuals, and then when they pass from the scene, the companies don't do very well. One of our father's strengths was that he attracted strong people who wanted to be associated with him. There was an inner security to him. These people were cantankerous, sometimes. But they were very successful.

So this company has never been dominated by any one individual. It's been a shared, collegial type of business, which it remains to this day." [17]

During the interview, Philip explained that early in his career he expressed concern regarding his share in the firm. "I made the mistake of talking about percentages to my father. I was complaining about not getting more of a percentage than I was. He said, 'Don't talk to me about percentages. A hundred percent of nothing is nothing!' His point was that if the firm grows and prospers, everyone will participate. That philosophy guides the firm today. So now we have 16 partners." [18]

The Lifestyle Objective

Wayne Hummer's goal was to nurture the brokerage business while continuing to run the LaSalle bank and maintaining involvement in civic affairs. Unlike many persons entering the securities industry, Hummer was

not looking for fame or fortune. Hummer did not believe in trying to make speculative gains in the short run. Consequently, his investment advice appealed to customers who planned to buy a security and hold it for the long run. That being the case, his firm could be and was run in a conservative and orderly fashion.

Wayne spent Monday through Thursday in Chicago helping with the affairs of the brokerage firm. On Thursday, after the close of the market, he would take the train home to LaSalle. Wayne spent Friday and Saturday at his desk in the bank and then, after taking his wife to church on Sunday, would visit the Hummer Insurance Company and return to the bank. Commenting on his weekend schedule, Wayne said in 1977, "I'd rather go down to the bank than play golf." [19]

Throughout his career, Wayne considered himself primarily a commercial banker. "I'm no broker," he stated in an interview with the Chicago Daily News. "I'm just a small-town banker." [20] A few months prior to his death in September 1980, Wayne was honored in LaSalle for his 73 years in banking.

Conclusion

Wayne Hummer and Company is an anachronism in the securities industry. It is reported to be the ONLY full-service firm with a seat on the New York Stock Exchange which does not buy and sell securities on its own account. The reason it does not is that the founder believed that doing so was unethical.

The firm is unusual also in its refusal to encourage short term speculation by customers, its shunning of aggressive salesmanship and its policy of restricting new hires to persons with the potential to become partners. Again the reason is the founder's ethical beliefs.

The net effect of these policies has been to create a firm where principles take precedence over profit, where an atypical calmness reigns, and where the partners truly perceive themselves as performing a useful service for the customer. By adhering to principles, Wayne Hummer deliberately resisted the temptation to make "big" money. What he got in return was a comfortable standard of living; an atypical atmosphere of collegiality at the office; and an atypical feeling of engaging in a worthwhile purpose.

The key to the firm's business success was the selection and servicing of a specialized market niche. As Wayne put it, "Safety and security are the main things we emphasize. That policy inspires confidence, and confidence is the mainstay of our business." [21] The key to the ethics success was probably Wayne Hummer's amazing sense of perspective. As he put it, "I'm just a small town banker."

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The Wayne Hummer and Company Code of Business Conduct, 1989

1. Our most important strengths are capital and remaining a partnership.
2. Wayne Hummer & Co. is a broker, not a market maker – i.e. we own no stocks or bonds for resale and therefore we are not exposed to any underwriting commitments.
3. Our basic investment philosophy is to buy and hold good grade securities of leading, financially secure and well-managed companies operating in essential industries with the proper diversification and balance between equities and fixed income securities.
4. As brokers for many banks, attorneys, corporations, profit sharing funds, individual investors and others, we are committed to the highest standards of quality service at all times, beginning with complete respect – by the Partners and the entire staff – for the confidentiality of all transactions.
5. We have a policy of no active telephone solicitation to buy securities.
6. As securities' custodians under wills and trusts, we have actively urged countless individuals across the nation to consult their attorneys to establish family revocable living trusts to avoid probate proceedings.

Trusted Financial Advice Since 1931™

Every February 16, we proudly celebrate the anniversary of the day we first opened our doors to serve the needs of the investing public. Although we now represent ourselves as Wintrust Investments, our roots run deep and we continue to live and work by the values upon which our firm was built in 1931 as Wayne Hummer & Company.

Wayne Hummer and George Barnes brought these qualities to bear in founding the firm. Both were successful commercial bankers who saw, in the midst of the Great Depression, a remarkable opportunity for a service firm that could provide small- and medium-sized banks with sound, long-term investment advice. Joined by LaSalle Street veteran, Harry A. Baum, they articulated a business philosophy based on integrity, quality, and dependability; a philosophy that was ahead of its time and quickly began to win clients.

We continue to hold ourselves to the highest standards of ethics and integrity first established by Wayne Hummer, and to pursue the long-standing mission of providing trusted financial advice with an uncommon level of personal service and attention.