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MEMORANDUM FOR MR. KENNEDY:

Summarizing the studies and investigations preceeding the enactment of Section 11 of the Act as clarified by the testimony of specialists and traders on September 11 and 12 suggests the following considerations:

(1) The question of permitting the floor trader to trade at all.
(2) The question of permitting the floor trader to execute orders for the accounts of others.
(3) The question of regulating not only his activities under Section 11 but dictating his margin obligations under Section 7.

Experience suggests most emphatically first, that the floor trader should be permitted freedom of general trading; secondly that he should be denied the privilege of executing orders for the accounts of others and third that he should be very strictly regulated to control the volume of his transactions, and most particularly that he should be held most strict in his margin requirements.

It is herein being assumed that the specialist will not be permitted to trade for his own account. All of those benefits which the specialist contends flow from his activities to provide liquidity in security markets are shown pretty conclusively to be far more dependent upon floor traders' activities than on specialists' activities. In practically every instance the specialists' purchases were an insignificant portion of the total transactions and practically never effective in stopping a break. Floor traders on the other hand, buying many times as much stock as the specialist, furnish a shock absorber at critical times and while they did not prevent disastrous breaks, they did provide some sort of market all the way down.

Because of the benefits which the specialist should provide but actually are provided by the floor trader, it would seem that genuine good is done for the speculative and trading public by permitting floor traders' operations.

Secondly, it seems most important to prohibit floor traders from executing orders for others. Operation of floor traders creates an audience and following for them, not only on the floor, but all over the speculative world. If the floor trader sells a large block of stock under cover for banking interests not only are floor traders who witness the transaction deceived, but commission house customers (the general public) who ask for an explanation of all important transactions are similarly deceived. Wrong conclusions are unavoidable and losses are most certain to result on trades initiated by the knowledge of the floor trader's transaction.

Thirdly, floor traders' activities should be strictly limited and particularly by being confined in volume to such transactions as are always adequately specifically margined. In addition the Exchanges themselves can be compelled to restrict excessive trading which would unduly excite a professional and public following.

Thus, in summary of the two days' meetings, it would seem a fair conclusion to say that by prohibiting specialists from trading for their own accounts and prohibiting them from revealing the contents of their books, undue advantages are removed from one class of floor traders and by permitting member brokers who may be floor traders or office traders to trade only for their own accounts, support and sustenance is given to the market in substitution for that which the curbing of specialists removes. Strict regulation of the actual trading operations thus permitted would follow unavoidably and is purely a detail of administration.

J. A. Fayne.

September 13, 1934.