

FIRST PROGRESS REPORT

INVESTMENT BANKERS
CODE COMMITTEE

December 6, 1934

Investment Bankers Code Committee

1010 Vermont Avenue

Washington, D. C.

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FIRST PROGRESS REPORT

TO ALL REGISTERED INVESTMENT BANKERS AND
ASSESSORS TO THE INVESTMENT BANKERS CODE:

I—Developments to Date

Now that the Code Committee has been in operation for seven months, it is time to take stock of our surroundings, to see what we have accomplished, to appraise the cost and to see, if we may, what benefits have been brought to the industry as a whole by the adoption of the Code, and what more we may do to further its usefulness to the public and to the trade.

The first task before the Committee was one of formulation of the Fair Practice Amendment which required frequent prolonged meetings and discussions. The second was one of organization; the third of interpretation; the fourth of administration. After the actual formative period of the Code the task of organization was undertaken. The Code applies to all dealers in the United States, irrespective of their consent to its provisions and is made binding on them by a Federal statute, namely the National Industrial Recovery Act. The Code Committee was selected according to the plan approved by the President of the United States, to administer the provisions of the Code, its actions being at all times subject to review by the National Recovery Administration. The necessary machinery for administration was provided through the election of seventeen Regional Committees, all the members of which Committees serve without pay, as do the members of the Code Committee.

The Regional Committees having been elected, the Committee turned to the next significant feature of the Code—Registration. The Code provides for voluntary registration which carries with it certain obligations as well as privileges. Up to this time 2977 dealers have registered, although by action of the Code Committee, November 1, 1934, eighty-three of these were dropped from registration for non-payment of the first assessment—after due notice and hearings conducted in accordance with the provisions of the Code. Complete lists of those registered (including cancellations) have been furnished to all Registered Dealers.

A further step in organization was the subdividing of the work into necessary committees for study and recommendation to the Code Committee for action. Therefore

an Executive Committee was established to function between Code Committee meetings and committees established on Finance, Interpretations, By-Laws, Fair Trade Practice Complaint Procedure, and for the purpose of co-operation with the Securities Exchange Commission.

Almost immediately the Committee was confronted with requests from nearly every State in the Union for explanations and interpretations of the Code. Many answers were given by the Managing Director, Counsel and Regional Committees to questions involving explanations of the language of the Code—but questions which involve interpretations must be passed upon by the Code Committee as a whole and approved by N. R. A. before release. To date several interpretations have been made by the Code Committee and one has received official approval by N. R. A.

Nevertheless the Interpretations Committee has held six meetings in the past three months for the purpose of drafting proposed amendments to the Code covering such vexing problems as 'beating the gun,' concessions to registered banks, meaning of 'three day clause,' concessions on old issues, confirmations at net prices, and others. Amendments covering the first three items as drafted by the Interpretations Committee have been adopted by the Code Committee and are now pending before the N. R. A.; the remaining two items and others are receiving further consideration by the Interpretations Committee.

On the subject of compliance the necessary forms and instructions have only recently received the approval of the N. R. A. and been distributed to Regional Committees. The Code Committee considers the close co-operation of Regional Committees to be of the utmost importance in this respect. The spirit of the Code calls for frankness and a universal desire to live up to its high principles of ethics and in many cases Regional Committees have been able to settle inadvertent violations and complaints without recourse to formal legal procedure. Where such is not the case, however, it is important to follow carefully the procedure outlined.

The Code Committee has endeavored to establish strong Regional Committees in all districts, for it is obvious that the Code will succeed only if Regional Committees are efficient. Approximately 30 per cent of all registered dealers have their home office in the New York district. In view of the importance of this investment center, arrangements were made for an executive secretary, who is also Deputy Managing Director of the Code. Such an organization

entails additional expense, but the Committee has confidence that its benefits are unquestioned.

With further reference to compliance, the Committee has instigated an investigation into the distribution of certain recent national issues and also has before it several complaints. Investigations by the Committee through the tracing of bond numbers of a syndicate issue and the taking of testimony in regard to other complaints are still under way. It would be unfair to make any detailed statement at this time.

II—Finances

With respect to finances, the Treasurer reports the following expenses of the Committee to September 30, 1934:

Originating Expenses:

Legal Expenses and Professional Services..	\$37,917.25
Investment Bankers Association.....	23,499.02
Code Committee—Travel and Meetings.....	9,229.30

\$70,645.57

Operating Expenses:

Salaries	\$16,757.25
Office Rent	875.00
Printing and Stationery.....	3,936.57
Incidental Office Expenses.....	151.00
Postage	1,684.12
Telephone	917.59
Telegraph	473.47
Traveling Expenses—Office.....	748.67
Legal Expenses.....	5,395.29
Expenses of Treasurer's Office.....	200.00
Accounting Expenses.....	597.08
Bond and Insurance Premiums.....	157.00
Office Equipment.....	2,234.70
Code Committee—Travel and Meetings.....	4,101.90
Regional Committees Expenses.....	10,029.81

\$118,905.02

The receipts from Assessment No. 1 to the same date were \$135,980, leaving a balance after the above expenses of \$17,074.98 against which were estimated unreported expenses of \$4,779.82. Outstanding bills receivable as of the same date were \$20,320.00.

Of the foregoing items of expenses \$70,645.57 was for

'Originating expenses,' that is to say for expenses incurred in the preparation and presentation of the Code and Fair Practice Amendment—this amount being approximately \$13,500 less than originally budgeted for such expenses.

Of the operating expenses many items are dependent upon the amount of general communications necessary to be made to the trade at the time of registration or the making of assessments, both of which require considerable expenditures for printing, stationery, billing and postage. The principal items may be commented upon as follows:

(1) Salaries—\$16,757.25.

The Committee considers this a reasonable amount for practically five months of the formulative period of a broad venture such as is the Code.

(2) Legal Expenses—\$5,395.29.

This sum, paid to counsel for services and expenses represents practically five months concentrated work on the Code, including many requests for interpretations, conferences with N. R. A., drafting registration procedure, By-Laws and Trade Practice Complaint Procedure and consultations with and advice to the Code, Finance and Interpretations Committees, the Executive Committee, the Managing Director and his staff.

(3) Code Committee Travel and Meetings—\$4,101.90.

This sum represents actual expenditures and an unreported amount estimated at \$979.82 may be added to it. The Code Committee contains twenty-one members, located in the cities of San Francisco, Los Angeles, Seattle, Denver, New Orleans, Baltimore, Minneapolis, Chicago, Louisville, St. Louis, Cleveland, Boston, New York, Philadelphia, Washington and Atlanta. Obviously the amount of traveling is great. The cost of one meeting of the Committee is from \$1,200 to \$1,500, or possibly more, depending upon location and attendance. All the members must carry their expenses themselves, sometimes for several months before reimbursement is possible through authorization of the Finance or Code Committees.

(4) Regional Committee Expenses—\$10,029.81.

This item may also be increased by requisitions from

twelve Committees whose combined budgets totaled \$3,500 for the months unreported. It is, however, far less than the original budget of \$24,000 to July 31st for all Regional Committees and less than the new budget to December 31st because of the uncertainties of expenses incident to enforcement and because Regional Committees themselves have conservatively over-estimated on account of lack of experience.

The Committee has arranged for an audit of the Treasurer's accounts by Messrs. Price, Waterhouse & Company as of December 31, 1934.

Under the N. R. A., Code authorities are required to have their budgets approved before spending the money collected. As will appear from the foregoing expenses, our estimates for Budget No. 1 were too high and we were able to operate for more than two months beyond the expiration date of that budget, July 31st, before calling for a new assessment. Budget No. 2, to run from July 31st to December 31st, 1934, is as follows:

BUDGET NO. 2.

(a) Salaries:

Managing Director	\$8,333.40
Deputy Managing Director....	2,083.40
Assistant to Managing Director	2,083.40
Comptroller	1,666.70
Sten. & List Clerk.....	758.40
Stenographer	700.00
Stenographer	625.00
Sten. & Telephone Operator...	500.00
File Clerk	500.00
Typist & List Clerk.....	500.00
Office Boy	325.00
	\$18,075.30

(b) Office Rent	875.00
(c) Printing and Stationery	3,000.00
(d) Incidental Office Expenses	250.00
(e) Postage	1,750.00
(f) Telephone	1,250.00
(g) Telegraph	1,000.00
(h) Traveling expenses—Office	1,000.00
(i) Legal Expenses	3,125.00
(j) Expenses of Treasurer's Office.....	500.00
(k) Accounting and Auditing Expenses.....	1,000.00

(l) Office Equipment	500.00
(m) Code Committee—Traveling and Meetings.	6,000.00
(n) Complaints and Investigations.....	15,000.00
(o) Seventeen Regional Committees.....	29,000.00
(p) Contingencies	5,000.00
	<u>\$87,325.30</u>
Credit available from collection of first assessment	34,930.00
Net amount to be raised by Assessment No. 2	<u>\$52,395.30</u>

It is to be noted that Budgets are not expenditures and the fact that an item is budgeted does not mean that it will be spent within the budget period. Our experience with Budget No. 1 proves this. Excess receipts tend to put off the time when the next assessment will be made, and due to our having a surplus as of September 30, as shown on page 5, and the further fact that we have collected a substantial amount of the unpaid bills outstanding as of the same date, the Committee anticipates that it will be in funds for some months of 1935. Budget No. 2, is, however, drawn only until December 31, 1934, and any surplus carried over beyond that date will be credited against our next budget.

Budget No. 2 contains some items upon which the Finance Committee could only hazard a guess. Such items as salaries, rent, traveling, ordinary legal expense, stationery, telephone and telegraph, are round amounts based upon previous experience and are only variable to a moderate extent, depending largely upon whether a new registration list is called for or a new assessment made during the period in which cases communications to all dealers, or at least to all registered dealers, are required.

On the other hand, the budget contains items for Regional Committees (\$29,000) and Investigations and Complaints (\$15,000) which may be highly variable. The former is based upon the budgets submitted by 17 Regional Committees and has proven greatly excessive to date. It is reasonable to expect that Regional Committee expenditures will be materially increased as these Committees become more active. The latter is purely a guess. Both these items would obviously be subject to wide fluctuation if business should increase, or if the public should learn to appreciate the value of Code protection, in either of which cases the work and expense of investigation, education and

compliance would undoubtedly increase. The Committee asked this protection from dealers in order that it might be in a position to meet these contingencies. In no event will it spend money it does not have. Again we repeat that items budgeted are not necessarily items spent.

Assessment on a personnel basis was chosen after a careful examination of other bases, such as on earnings, capital, profits and business done.

III—Benefits of the Code

With reference to the effectiveness of the Code itself, the Committee feels that much has been accomplished. The organization is now equipped to function. It is for the dealers to offer wholehearted co-operation to the end that the ideals upon which the Code is founded may be learned, understood and effectuated throughout the industry. The General Principles constitute a pledge to the public to conduct our business on "high standards of commercial honor" and the realization of this end calls for teamwork of the highest order.

The rules governing new issues of securities assure to dealers and to the public more adequate information than heretofore required and the sections covering selling syndicates and groups in connection with new issues are designed to decelerate the process of distribution in the interest of more mature consideration of new issues by both dealers and their clients. No section of the Code was more difficult to write and probably no section has caused more misunderstanding and confusion as to its meaning. The Committee has, as noted above, adopted and submitted to the N. R. A. several amendments and is in the process of offering others which it is hoped will clear up the difficulties. Certainly such provisions, when clarified and understood, should work substantially to the advantage of dealers.

The one-price feature of the Code is for dealers the most effective and beneficial provision even in these times of dull business. For many years, the industry has literally been giving away substantial amounts of money in discounts and the Code provides a means by which this practice can be remedied. To date, most of the gain in this respect has been through distribution of public securities but when the general capital market is again reopened the advantage is obvious. Even under present conditions the Committee feels that if dealers will check their transactions they will find from this one source a benefit many times exceeding their share of the cost of administering the Code.

The Committee desires to call attention to the requirements as to supervision of sales made by salesmen. It is most desirable that houses take advantage of the present dull times to set up adequate methods of checking such sales in order that the system may be workable in more active markets. The provisions as to employment of salesmen have been generally satisfactory. They tend to require experience and qualification in order that only proper representatives may solicit business from the public. Many of the Regional Committees have had occasion to operate under these provisions and those representing several districts have developed a method of written examination for prospective salesmen, which method should be most helpful in assuring a fair test. The language concerning solicitation at residences without prior written consent of the parties to be approached has been open to some question, but the Committee believes that the spirit of the provisions is clear and that dealers must conduct themselves in conformity with that spirit in order that our industry may not be brought into disrepute through the wholesale solicitation of people at their homes by personal calls or by telephone without first obtaining written permission so to do. The activities of other salesmen do not constitute a defense for solicitations of this character and when formal complaints are filed the Committee may be forced to act under the General Principles as well as the specific language of Article VII, Section 3.

Some of the benefits of the Code are undoubtedly lost through lack of coordination within dealers' offices. Communications from the Managing Director or the Code Committee should be routed regularly to the appropriate partners or employees. The same has also been true of the passage of information to branch offices by home offices. All registered dealers should understand that communications from the Managing Director or Code Committee are sent only to home offices and it is the responsibility of such offices to keep their personnel informed, wherever they may be located. This is particularly important because of the possibilities of violations by branch offices due to lack of information.

The Registration provisions have gone into effect as already noted and the Committee is now engaged in surveying the list in order that it may contain only the names of those who believe in the Code and are able and willing to live up to its obligations. From time to time amended lists are issued and the Committee asks the earnest co-operation

of all dealers in making this feature of the Code useful and effective.

There remains the question of compliance. We already have before us instances which indicate that dealers and the public are beginning to realize the advantages of Code protection. Complaint procedure forms and instructions have already been issued, supplementing the language of the Code in this respect. The task will be greatly simplified if all dealers will study the Code and Procedure carefully. The Committee hopes that dealers will consult freely with their Regional Committees in order that violations may be avoided. In cases of wilful violation, however, the Committee of course will take punitive action in accordance with the Procedure for handling Trade Practice Complaints.

In general, the Committee feels that much progress has been made. The complications of operating under a Federal Statute have required that we proceed slowly but now that the formulative period is passed, we look to the dealers of the country to offer their generous assistance in working under the principles which we have adopted for ourselves for the good of all. Our problem now is to realize the advantages of those principles, to follow them carefully and to thus prepare ourselves for the expansion of our business which is essential to the country. Although this memorandum is a report by the Code Committee covering its activities to date, it would fail in its purpose if it did not point out to all those whose activities come under the provisions of the Code that this is their Code. The Code Committee and the Regional Committees are their representatives and cannot expect to serve the best interests of the business unless they receive from the dealers suggestions, opinions and criticisms. Only with the wholehearted support of the dealers who have created and subscribed to the principles adopted can the Committee accomplish the purposes of the Code.

Yours very truly,

INVESTMENT BANKERS CODE COMMITTEE,

by ROLLIN A. WILBUR,
Managing Director.

December 8, 1934.