

March 21, 1935.

Mr. Richard Whitney, President,  
The New York Stock Exchange,  
New York, N. Y.

Dear Mr. Whitney:

I am submitting herewith a memorandum setting forth the viewpoint of the Securities and Exchange Commission as to the suggestions made by the New York Stock Exchange in answer to the eleven recommendations contained in the Commission's report to Congress.

Very truly yours,

Joseph P. Kennedy,  
Chairman.

The first and second recommendations of the Commission suggested that a better numerical representation of the commission broker who possesses direct contacts with the public should be had on the governing committee, and that office partners of registered firms should be eligible for membership on the governing committee. The Commission has already expressed itself to the effect that the proposal of the New York Stock Exchange to increase its Governing Committee to 48 by adding 8 non-member office partners seemed a satisfactory solution of the problem presented by the second recommendation. The addition of these governing members, even though such members are not required to be office partners of commission brokerage houses, will offer increased opportunity for the representation of commission brokers and thus tend to effectuate the general objective stated in the first recommendation.

The third recommendation of the Commission was to the effect that nominations to the Governing Committee should be by petition and not by the device of a nominating committee. The Commission pointed out in its report that the present method of selecting a nominating committee tended towards self-perpetuation of the "in" group, both as regards the nominating committee and the Governing Committee. Representations have been made to the Commission that the continuation of some type of nominating committee is desirable, in that it promotes, as against the method of nomination by petition, a continuous study and scrutiny of candidates for officers and for the Governing Committee, thus resulting not only in individually more desirable candidates but also a better balanced group of candidates. The

Commission deems that the device of a nominating committee may have merit, provided that the possibility of perpetuation of control is guarded against by a change in the method of selecting the nominating committee.

The Exchange has suggested that in lieu of the present method of a nominating committee of five, which annually nominates five members to constitute the nominating committee for the following year, certain changes should be effected. The Exchange suggests that the nominating committee shall be increased to seven members elected annually from a slate of fifteen proposed by the preceding nominating committee; that additional candidates can be proposed by the existing method of petition, which candidates will be added in alphabetical order to the list proposed by the outgoing nominating committee, thus affording no outward mark of distinction between those candidates nominated by the nominating committee and those nominated by petition; and, also, in order to permit the membership to judge as to the representative character of the nominees, descriptive words such as "specialist," "floor broker," "odd-lot dealer," etc., should be added after the name of each nominee.

The Commission believes that this procedure deserves, at least, a fair trial before doing away with the nominating committee as a whole. It believes, however, that, to better safeguard against the possibility of perpetuation of control, the proposed committee of seven should be elected from a slate of twenty-one rather than of fifteen.

The right of nominating members to the Governing Committee by petition as heretofore is to be preserved, and the method of arranging

these nominees in alphabetical order, as will be true in the case of nominees for the nominating committee, should be continued.

The fourth recommendation of the Commission was that one-third instead of one-fourth of the members of the Governing Committee should be elected annually. To this the Commission is of the opinion that no adequate reason has been given for not adopting the Commission's proposal. This matter, however, is to be given further consideration by the Exchange, owing to the fact that mechanical difficulties are involved in making this change.

The fifth recommendation of the Commission suggested that the President should be nominated by petition. This recommendation is naturally consistent with the third recommendation of the Commission. If the changes suggested above in response to the third recommendation are effected, the Commission similarly believes that the objective sought by this fifth recommendation may equally well be attained through the proposed procedure for revising the method of selecting a nominating committee. Furthermore, the Exchange proposes to permit absent members to vote in all elections by ballot in like manner as absentee voters are permitted to vote in some states.

The sixth recommendation of the Commission suggested that membership on the Exchange should not be a necessary condition to eligibility for the office of president as well as other executive offices. Though the

Commission noted in its earlier report that, because of the public interest now being represented by the Commission, no present necessity existed for insisting upon the abandonment of membership as a condition of eligibility to office, it did observe that the abandonment of that condition on some of the major exchanges would seem to create no essential disadvantages, and would make available for that post a possible outstanding figure who might not happen to be a member of the exchange. The choice as to whether an exchange at any particular election should or should not go outside its membership for these officials should, of course, be left to the exchange, but the existence of such a restriction of eligibility in the constitution of an exchange tends to make its members fail to consider the possibility of securing non-members of the exchange for important offices. The Exchange is now considering the entire problem with its many implications.

The seventh recommendation of the Commission suggested that membership on the standing committee should not be restricted to members of the Governing Committee. The Exchange has removed any restriction of this nature that its Constitution may have seemed to impose upon the membership of standing committees.

The eighth recommendation of the Commission suggested that the expenses of arbitration should be reduced. The Exchange believes that the expenses have hitherto been moderate. It proposes, however, to take measures to effect this end.

The ninth recommendation of the Commission suggested a change in the arbitral tribunal in cases where one of the parties to the arbitration was not a member of the exchange. The right to arbitration before the arbitration committee of the exchange is at present granted to any customer regardless of the contract between the member and the customer. Since the customer can at any time prior to arbitration choose to seek his remedy in the courts, continued maintenance of this policy possesses no disadvantage, provided that the Exchange also encourages arbitration before independent arbitral tribunals as an additional remedy available to customers. The simplest manner by which to accomplish this end would be for the Exchange to encourage its members to offer customers a standard arbitration agreement requiring that resort be had to arbitration at the election of either the customer or the member, and providing for arbitration before independent arbitral tribunals at the election of the customer.

The tenth recommendation of the Commission suggested that adequate and effective appeals should lie from the business conduct committee to the Governing Committee. The Exchange proposes that a special advisory committee of three governors should be appointed to examine the record on appeal in each case and to give an advisory opinion to the Governing Committee. The appellant, whether a member or a non-member, shall have the right to designate which three members of the Governing Committee shall act as the special advisory committee on his appeal, but if he should fail to appoint such an advisory committee at the time of filing notice of appeal, the presiding officer of the Governing Committee shall designate three members

to serve as such special advisory committee. This method is to be applied also to appeals taken from the decisions of the arbitration committee as well as the other standing committees. The proposed procedure promises well.

The eleventh recommendation of the Commission suggested that customers preferring complaints against members should be furnished with the answer made by the member to the customer's complaint, should be entitled to appear before the committee, and that both parties in these cases should have the right of appeal to the Governing Committee. The Exchange proposes that the business conduct committee will, in cases where all the facts and conditions are not readily ascertainable without a hearing, give complainants an opportunity for a hearing, and further proposes that the right of appeal shall be accorded complainants in the manner set forth under the tenth recommendation. It also proposes that the complainant shall be furnished with the substance of the answer, or, in cases where the legal rights of the member would not be prejudiced, with a copy of the answer. Furthermore, the complainant will then be given time to offer additional evidence or proof in rebuttal before the hearing or disposition of the case. The success of such a procedure obviously will depend to a considerable degree upon the careful and faithful summarization of answers when the complainant is not furnished with a copy of the answer. But the procedure would seem to be adequate to effectuate the purpose of the Commission's recommendations.