IN THE

United States Circuit Court of Appeals

FOR THE SECOND CIRCUIT

SECURITIES AND EXCHANGE COMMISSION,
Appellant,

v.

CHINESE CONSOLIDATED BENEVOLENT ASSOCIATION, INC.,
Appellee.

ON APPEAL FROM THE DISTRICT COURT OF THE UNITED STATES FOR THE SOUTHERN DISTRICT OF NEW YORK.

BRIEF FOR DEFENDANT, CHINESE CONSOLIDATED BENEVOLENT ASSOCIATION, INC.

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Dated, April 3, 1941.

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Statement of Facts

The facts are undisputed, all facts alleged in the complaint having been admitted by the answer. In fact, the complaint is based upon an agreed statement of facts entered into by stipulation between counsel for the parties hereto.

Chinese Consolidated Benevolent Association, Inc.,* is a membership corporation organized under the Laws of

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*For convenience, we will refer to the Chinese Consolidated Benevolent Association, Inc., as the "Defendant", the Securities and Exchange Commission as the "Commission", the Securities Act of 1933 as the "Act", the Government of the Republic of China as the "Government", the 4% Liberty Bonds of the Twenty-sixth Year of the Republic of China and the 5% United States Dollar Bonds as the "Liberty Bonds" and the "Dollar Bonds", respectively and collectively, as the "Bonds", the General Relief Fund Committee as the "Committee" and New York Agency of the Bank of China as the "Bank".

the State of New York, having a membership of approximately 25,000 Chinese who reside in or near New York City (R. 5).

Defendant is a charitable organization, its objects, as set forth in the certificate of incorporation, being—

> "To ameliorate the condition of the Chinese poor in and about the City of New York.
>
> "To care for and help sick and destitute Chinamen in and about the City of New York.
>
> "To give advice and pecuniary assistance as required to reputable and deserving Chinamen in and about the City of New York.
>
> "And generally to aid and succor all worthy Chinese who may be found to be in need of assistance."

and performs many functions in aid of the Chinese here. Defendant and its members are, of course, intensely interested in all matters relating to their mother country.

The Committee was organized in October, 1937, for the following purposes (R. 6):

> (a) to unite the Chinese community and the various organizations and societies thereof in aiding the Chinese people and the Government of China in their difficulties and to bring about concerted efforts toward that end;
>
> (b) to inform the Chinese people in New York as to the true state of affairs in China, to correct misrepresentation as to such conditions and affairs and to combat misinformation and false propaganda;
>
> (c) to solicit and receive funds from members of the Chinese communities in New York, New Jersey and Connecticut and from the general public in those states, for transmittal to China *for general relief* purposes. (Italics ours.)

Its members reside in the City of New York, are leaders in the Chinese community and serve voluntarily, having at

no time received or expected to receive compensation for their services (R. 6).

Neither the Committee nor any of its members has any official or contractual connection with the Government or any branch thereof (R. 6).

In 1937, prior to the organization of the Committee, the Government authorized the issuance of the Liberty Bonds and in 1938 the Government authorized the issuance of the Dollar Bonds. No registration statement pursuant to the Act as to the Bonds has ever been in effect (R. 5).

The Committee has from time to time held mass meetings at which information has been given out as to conditions in China and has made reports as to the results accomplished by it. Through the medium of such mass meetings, by personal appeals and by means of newspaper advertisements, the Committee has urged members of Chinese communities in New York and vicinity to purchase the Bonds (R. 6-7).

In some instances, at the request of and for the convenience of prospective purchasers of the Bonds, the Committee has received funds from prospective purchasers, has delivered all of such funds to the New York Agency of the Bank of China for the purchase either of Liberty Bonds or Dollars Bonds for the account of the respective prospective purchasers and has delivered a receipt for the funds so received to the person from whom it received them (R. 7). In all cases in which it has received funds the Committee has filed applications in the name and on behalf of prospective purchasers for the purchase of the Bonds and has obtained receipts for the funds delivered to the Bank (R. 7). The Committee has acted as an agent for the prospective purchasers only to the extent of delivering funds received from them to the Bank. Upon receipt of applications, whether made personally by, or by the Committee for, prospective purchasers, the Bank has transmitted the funds received by it to its Agency in China with instructions to purchase the Bonds for the account of the prospective purchasers (R. 8).

Upon receipt of the Bonds, the Bank has delivered them to the individual purchaser in accordance with his name and address appearing on the Bank's receipt. The Bank acts solely as an agent and makes no solicitation of the purchase of Bonds or for the business involved in transmitting the money for the purchase thereof (R. 8).

No charge is made by the Committee for its services in connection with receiving funds to be used for the purchase of Bonds and all such funds are delivered by it to the Bank for remittance to China. The members of the Committee receive no compensation, either from the persons who transmit money or from the Bank or from the Government or any department or agency thereof or from any other source in connection with its activities (R. 9).

The Question Involved

The sole question involved on this appeal is whether Defendant is an "underwriter" within the meaning of that term as defined in the Act.

The learned Court below has properly answered this question in the negative (R. 37).

ARGUMENT

We deem it desirable to point out to the Court certain fundamental considerations which we believe the Court should have in mind in considering the question presented by this appeal.

First, *there is and can be nothing to prevent the Government from selling the Bonds in China.* In this case all Bonds are sold in China.

Second, *no individual is or can be prohibited from purchasing Bonds from the Government in China.* The facts in the instant case clearly show that all purchases of Bonds are made in China by agents of the individual purchasers.

Third, *neither the Defendant nor the Committee is an agent in this country of the Government.*

Fourth, the activities of the Committee in urging others to buy the Bonds are entirely distinct from its activities as agent for prospective purchasers and must be so considered. These activities must not be confused.

Fifth, all sales of Bonds take place in China.

POINT I

Defendant is not an underwriter within the meaning of that term as defined in the Securities Act of 1933.

In this action the Commission sought to enjoin the Defendant from certain acts and practices which are alleged to violate Section 5(a) of the Act, which reads as follows:

> "Sec. 5. (a) Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly—
>
> "(1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell or offer to buy such security through the use or medium of any prospectus or otherwise; or
>
> "(2) to carry or cause to be carried through the mails or in interstate commerce, by any means or instruments of transportation, any such security for the purpose of sale or for delivery after sale."

This section does not apply to all transactions in unregistered securities, certain types of transactions being exempted from the prohibitions of this section by Section 4(1), which provides in part as follows:

> "Section 4. The provisions of Section 5 shall not apply to any of the following transactions:
> "(1) Transactions by any person other than an issuer, underwriter or dealer;"

Since it is not claimed that Defendant is either an issuer or a dealer and since, in fact, it is neither (R. 35), unless Defendant is an "underwriter", the provisions of Section 5(a) are not applicable to it and the action must fail.

Used in its technical sense, the term "underwriter" was, prior to the adoption of the Act, defined to mean one who for a commission undertook to see that an issue of securities was disposed of to the public at a price and to purchase such part of the issue as might not be taken by the public. As used in a popular sense, the term was also defined loosely to mean one who purchased all of an issue of securities and resold it for his own account to the public. In the technical sense, the underwriter acted under a contract or agreement with the issuer; in the popular sense, the underwriter purchased for himself and marketed the securities for his own account. In either sense, the term implied certain relationships between the underwriter and the issuer.

In the definition of the term which is contained in Section 2(11) of the Act, both the technical and popular definitions have been included. Such section, insofar as it is material to the issue on this appeal, reads as follows:

> "The term 'underwriter' means any person who has purchased from an issuer with a view to, or sells for an issuer in connection with, the distribution of any security, or participates or has a direct or indirect participation in any such undertaking, or participates or has a participation in the direct or indirect underwriting of any such undertaking."

It is clear in the present case that Defendant has not "purchased from an issuer with a view to, * * * the distribution of any security"; that is, Defendant is not an underwriter in the popular sense of the term (R. 35). Nor can there be any contention that it is a person who "participates or has a direct or indirect participation in any such undertaking, or participates or has a participation in the direct or indirect underwriting of any such undertaking".

Accordingly, the only question here involved is whether Defendant "*sells for an issuer* in connection with, the distribution of any security" (italics ours); i. e., is an underwriter in the technical sense. The determination of this question depends in turn on the determination of the questions (1) whether Defendant "sells", and (2) if so, whether it sells for an issuer".

A. Defendant's activities do not constitute "sales".

It must be clearly apparent that under any ordinary definition of the word "sell" Defendant's activities do not constitute sales.

The term "sell" has been defined in Section 2(3) of the Act as follows:

> "The term 'sale,' 'sell,' 'offer to sell,' or 'offer for sale' shall include every contract of sale or disposition of, attempt or offer to dispose of, or *solicitation of an offer to buy*, a security or interest in a security, for value; except that such terms shall not include preliminary negotiations or agreements between an issuer and any underwriter." (Italics ours.)

The only portion of the foregoing definition that can have any application here is the clause "solicitation of an offer to buy". A mere reading of the definition in connection with the facts of the case should be enough to cause one to discard all other provisions of this section.

In the first place, Defendant does not "attempt or offer to dispose of * * * a security" because it has no security to dispose of either by ownership or by the existence of any relationship with the issuer which would permit it to make such disposition, nor, in the second place, does Defendant contract to sell or dispose of a security (R. 35). As the learned Court below says in its opinion (R. 36):

> "The words 'attempt or offer to dispose of' a security connotes authority from the issuer to consummate the transaction, and in an effort to bring the defendant within that phase of the definition set forth in Section 2(3) of the Act the Commission begs the question in its reply brief."

Its activities in urging purchasers to buy the Bonds is purely voluntary on its part and made only on its own initiative. It is neither an agent of the Government nor of the respective purchasers in so urging. In delivering funds to the Bank for individual purchasers, Defendant merely acts as the former's intermediary, doing for the former what they could unquestionably do without in any way violating the Act.

Do Defendant's activities involve "a solicitation of an offer to buy"?

Although at first blush one might perhaps answer "yes", since it is undisputed that Defendant urges all Chinese to buy the Bonds, that is, asks them to make an offer to buy them, a careful analysis shows that it was never contemplated that the Act should be so broadly applied. The definition of the term "sale" is discussed in H. R. Rep. No. 85 (73rd Congress, 1st Session), in which it is said:

> "The term 'sale' or 'sell' is defined broadly to include every attempt or offer to dispose of a security for value. It includes within the definition of 'sale' an offer to buy, thereby preventing dealers from making offers to buy between the period of the filing of the registration statement and the date upon which such a statement becomes effective. Otherwise, the underwriter, although only entitled to accept such offers to buy, after the effective date of the registration statement, could accept them in the order of their priority and thus bring pressure upon dealers, who wish to avail themselves of a particular security offering, to rush their orders to buy without adequate consideration of the nature of the security being offered."

In discussing Section 5 of the Act with respect to activities of underwriters and dealers during the twenty-day waiting period, the Federal Trade Commission, the Commission's predecessor, in Securities Act of 1933, Release No. 70, November 6, 1933, referred to the foregoing report and said:

> "This period, says the House Report, contemplates a change from methods of distribution lately in vogue

which attempted complete sale of an issue sometimes within one or at most a few days. Such methods practically compelled distributors, dealers, and even salesmen as the price of participation in future issues of the underwriting house involved, to make commitments blindly.

"During the waiting period, as well as prior thereto, Section 5 of the Securities Act makes it unlawful for the issuers, underwriters, and dealers (to whose transactions the Act is generally applicable) to make an offer to buy or to sell a security—always remembering that 'sell' carries within it the conception expressed in Section 2(3) of an offer to sell or a solicitation to buy. The same section also makes it unlawful to transmit any prospectus (the central feature of which under Section 2(10) is the fact that it offers a security for sale) relating to a security during this period prior to the effective date of a registration statement. The purposes of these sections as related to this particular problem are obvious. Dealers are not to be solicited to buy the security until a registration statement is in effect; nor are they to offer to buy such security—an injunction made necessary by the fact that otherwise priority of application during the waiting period might be made the basis for priority of allotment."

From the foregoing, it is perfectly clear that the inclusion of the clause "solicitation of an offer to buy" in the definition of the word "sell" was meant to prevent the circumvention of the twenty-day waiting period provided by the Act by the establishment of priorities by an underwriter based upon orders obtained by it from, or submitted by, dealers prior to the expiration of such period.

The Commission, in its brief, is able to point to only one statement by the Commission in which the phrase "solicitation of an offer to buy" is discussed, that is, an opinion of General Counsel for the Commission contained in Securities Act of 1933, Release No. 1256, February 9, 1937. In such opinion, the General Counsel expressed as his opinion that the sending of circulars which certain security dealers proposed to send to holders of "called bonds" of a corporation to secure orders for the purchase

of new debentures to be issued by such corporation and offering the services of the dealers as "buying agents" to purchase them would constitute a "solicitation of an offer to buy".

Although we agree with the opinion of the Commission's General Counsel on the facts set forth therein, that opinion does not apply to the present case for the reason that in the opinion those who proposed to send the circulars were dealers and hence within the provisions of the Act.

Defendant's activities do not constitute *solicitations of offers* to buy.

B. Defendant is not selling "for an issuer".

If it is assumed for the purpose of argument that Defendant's activities in urging others to buy the Bonds constitute "sales", Defendant is an underwriter only if it sells the Bonds "for an issuer".

It seems to us clear that the use of the phrase "for an issuer" in conjunction with the word "sells" indicates the intention of Congress by this definition to define as an "underwriter" a person who fell within the meaning of that term as it was technically defined prior to the adoption of the Act; that is, that an underwriter is one who contracted with an issuer to sell to the public its securities and to take up such balance as might not be sold to the public. This is even more clear when it is realized that the clause now under consideration is the correlative of a clause defining as underwriters those who prior to the adoption of the Act fell within the popular definition; that is, persons who have purchased "from an issuer with a view to, * * * the distribution of any security".

Only those who "sell *for an issuer*" are underwriters.

Accordingly, as used in the Act, the term "underwriter" involves the existence of a contractual or agency relationship between the issuer and the person alleged to be an underwriter. To hold otherwise would negative the existence of any exemption under Section 4(1).

The Commission has in effect recognized that such a relationship must exist. In *Matter of Canusa Gold Mines, Limited,* Securities Act of 1933, Release No. 1507, July 15, 1937, the Commission held that an issuer was liable under Section 12(1) of the Act in connection with the sale of its stock prior to the filing of a registration statement therefor on the ground that a certain firm of brokers which sold such stock was an underwriter thereof. It appeared that directors and principal stockholders of the issuer loaned their stock to the brokers under an arrangement providing for the sale thereof to the public and the remission to the issuer of 25¢ per share from the proceeds of such sale. The Commission discussed the evidence at length and held that it had been established that such transaction had taken place with full knowledge of the issuer and as part of an arrangement between the issuer, its stockholders and the brokers. The Commission held that the stock was sold "for" the issuer, that the brokers were in fact agents of the issuer and hence that they were underwriters of the stock. The Commission said:

> "An 'underwriter' is defined by Section 2(11) of the Securities Act of 1933 as 'any person who * * * sells for an issuer in connection with the distribution of any security, or participates or has a direct or indirect participation in any such undertaking * * *'. It is clear that the sales by Outlook Investments, Ltd. of stock loaned to it by the officers, directors and stockholders of the registrant pursuant to a tripartite understanding between these persons, the underwriter and the issuer constituted sales 'for' the issuer, Canusa Gold Mines Limited in connection with the distribution of its stock. The fact that 25¢ per share of the proceeds of all such sales was paid direct to the registrant or applied to its account is conclusive that Outlook Investments, Ltd. was acting for the registrant in selling the loaned shares. Therefore, there can be no question that this distribution of the borrowed stock through the mails and in interstate commerce was effected by Outlook Investments, Ltd. *as an agent for the registrant* and *hence with respect to these borrowed shares it was an 'underwriter' as defined in the*

> *Act.* Unless some exemption under Section 3 of the Act is applicable to the securities sold, all transactions by an underwriter are subject to the registration requirements of Section 5(a) of the Securities Act. No such exemption is claimed in this case. Accordingly, all sales thus made by Outlook Investments, Ltd., directly and indirectly, through the mails or by the use of instrumentalities of interstate or foreign commerce seem to have been in direct violation of Section 5(a)(1) of the Act. Likewise the delivery of shares through these means for the purpose of sales or after sale would appear to have violated Section 5(a)(2). These transactions accordingly resulted in civil liabilities under Section 12(1) of the Act. Since these sales were effected for the benefit of, and under an arrangement with, the issuer who receivd 25¢ per share sold, it is our opinion that the civil liabilities thus created may extend to the issuer." (Italics ours.)

This states the law as we believe it to be, namely, that to be an underwriter one must act "for an issuer"; that is, as an agent of the issuer.

In the present case, Defendant has no contractual or agency or other relations with the Government or any of the latter's agencies (R. 35).

Under these circumstances, the learned Court below properly held that Defendant is not an underwriter and, hence, that no injunction should be issued (R. 37).

The fact that Defendant assists prospective purchasers of the Bonds in taking funds to the Bank and executing applications for the purchase of Bonds does not change Defendant's status in any way. This the Commission concedes (B. 11). It is doing merely what such purchasers could unquestionably do themselves without falling within the prohibitions of the Act.

Since Defendant is not an underwriter, it has the right of any individual to express its opinion concerning, and to urge the purchase of, the Bonds. Congress never intended the result for which the Commission contends, namely, that a person who neither has any connection with

an issuer nor sells for his own account is nevertheless an underwriter because such person urges others to purchase from the issuer the latter's securities.

The Act clearly was intended to apply to persons who are "underwriters" as that term was defined either technically or popularly at the time of the adoption of the Act. Defendant is not an underwriter under that definition or under the definition contained in the Act. To so find would result in the emasculation of the exemptions provided in Section 4(1).

POINT II

The Commission in its brief has utterly failed in its attempt to show that, on the facts stated in the complaint, Defendant is in any way violating the provisions of the Act.

In considering the arguments made by the Commission the Court should have in mind the fundamental factors set forth above (supra, 4-5).

The Commission's arguments are in essence that there is a sale or delivery after sale; that Defendant is not exempt under Section 4(1) of the Act because (a) Defendant's acts are a part of a "transaction by an issuer", and (b) that Defendant is an underwriter because it sells "for *the benefit of* the issuer" (italics ours); that Defendant should be enjoined because it is aiding and abetting a violation of the Securities Act; and that injunctive relief rather than recourse to diplomatic channels is the proper remedy.

One argument made by the Commission is worthy of some notice; that is, that a decision adverse to the Commission's contentions "would set a precedent which would be equally available to Germany, Italy or Japan" (B. 6)* and would open the way "for violations by other persons with less worthy motives" (B. 26). This argument is fur-

* References to the Commission's brief are noted as "B".

ther elaborated at page 21 of its brief. We earnestly submit that, although this argument might have some merit under certain conditions, it is of little weight today. The United States has a very effective weapon against the sales of German and Italian securities by its restrictions on the use of foreign exchange in connection with those countries. This restriction could also be applied to Japan in case of necessity. For this reason, we believe the argument of the Commission should have very little weight.

A. The Commission misstates and distorts the facts.

Although the facts alleged in the complaint and admitted by the answer were based upon a statement of facts agreed to by counsel for the Commission and for Defendant, we find it necessary before discussing the Commission's arguments to point out to the Court serious misstatements and distortions of the facts which we believe must have been inadvertent.

Although the record clearly states (R. 6) that—

> "Neither the Committee nor any of its members has any official or contractual connection with the government of the Republic of China or any branch thereof."

it is stated in the Commission's brief (B. 4) that:

> "*It does not appear that* the Committee or any of its members have any official or contractual connection with the Republic of China or any branch thereof" (R. 6). (Italics ours.)

This statement implies some doubt upon this matter where no doubt can exist.

The statement (B. 4) that Defendant "has been the medium through which * * * bonds * * * have been sold to residents * * *" and the statement (B. 17) that the Bonds are being sold to residents of the United States "through the medium of this Defendant" are entirely unsupported by the facts set forth in the complaint and admitted by the answer. No sales are made by or "through

the medium of" the Defendant. The sale is made by the Government in China. Defendant, on the one hand, urges the Chinese in general to purchase the Bonds and, on the other, at their request, acts as agent for individual purchasers in delivering funds to the Bank.

On the admitted facts, the statement (B. 4) that Defendant has used or caused to be used the mails "in delivering these securities after sale to residents of the United States" is wholly unfounded. The admitted facts show clearly that Defendant has no control whatsoever over the methods used for the delivery of the Bonds, that being solely in the control of the purchaser's agent in China. We do not concede that Defendant has in any way caused the mails to be used in the delivery of the Bonds after sale.

The statement (B. 7-8) that "* * * as a result of its activities, it has received orders * * *" is contrary to the fact. Individual purchasers have delivered funds to Defendant as their agent with directions to deliver such funds to the Bank and to execute applications on their behalf for the transmission of such funds to China for the purchase of Bonds there.

The admitted facts do not justify the statement (B. 14) that "in the final analysis the defendant is distributing securities for the benefit of the issuer". It does not distribute any securities. The learned Court below so found, stating (R. 35):

> "The described activities of the defendant clearly establish that defendant made no contract of sale and *no distribution of a security.*" (Italics ours.)

The admitted facts refute the statement (B. 15) that "there is no separate and distinct transaction carried through by the defendant; its solicitation merely initiates a transaction to be completed by the Republic of China". Clearly, on the facts stated, Defendant's action in urging the purchase of Bonds is entirely separate and distinct from the subsequent action taken by individual purchasers or by Defendant for them. As for initiating the trans-

action, the actual facts are that the individual purchasers initiate the purchase of the Bonds for their own reasons which may or may not be based upon Defendant's appeals. Defendant's action in urging the purchase of Bonds is entirely independent of the action of the individual purchasers in determining whether they should buy the Bonds.

The statement that (B. 20) "the defendant induces the purchase of Bonds from the Chinese Government and causes the transmittal of the entire purchase price to the issuer" is entirely unsupported by the facts stated. On such facts it is impossible to state what causes the individual purchasers to make such purchases. Could it not be that they desired to help their mother country regardless of Defendant's appeals? Could it not be that Defendant's appeals are nothing more than the appeals which each Chinese feels in his heart? In the foregoing statement the Commission confuses the two actions taken by Defendant, namely, (1) urging the purchase of the Bonds, and (2) acting as agent for individual purchasers. Of course, Defendant must, as agent for individual purchasers, cause the transmittal of all funds received by it to China. We are sure that the Commission will not contend that an individual purchaser could not do this himself.

The Commission's arguments (B. 20) as to the realities of the situation are wholly unfounded. Far from being the realities of the situation, the arguments made by the Commission are nothing more than figments of its imagination devised for the purpose of supporting an unsupportable argument. These statements are a perfect example of the Commission's attempt to confuse the Court by confusing the facts. The Commission concedes that, in determining whether Defendant is an underwriter and hence subject to the Act, the only activities to be considered are its activities in urging the purchase of the Bonds (R. 35). The Commission concedes that Defendant's activities as agent for purchasers has no bearing on this point (B. 11). It may be true that the Bonds are being purchased by

residents of the United States, but such purchase is made in China by the purchaser's agent and Defendant has nothing to do with the distribution of these Bonds.

The statement (B. 26) that "it is the agency primarily responsible for the distribution of Chinese bonds in this area" is an illustration of the distortion of the facts to which the Commission has found it necessary to resort in order to justify its position.

B. Defendant is entitled to the exemption provided by Section 4(1).

In Points I and II of its brief, the Commission attempts to show that Defendant is not entitled to the exemption set forth in Section 4(1) of the Act on the ground that it is participating in a "transaction by an issuer" and is an "underwriter".

In Point I of its brief, the Commission argues that Defendant is "selling" the Bonds and is causing them to be delivered after sale by means of the mails. What we have said in Point I, we think, effectively answers the Commission's argument (B. 7-11) that Defendant's activities in urging the purchase of Bonds constitute a "sale" as that term is defined in the Act. We must point out, however, that the Commission, in its argument, confuses these activities with Defendant's activities in delivering funds to the Bank as agent for various individual purchasers.

Contrary to the statement (B. 7) that Defendant claims that it has been acting as agent for purchasers in the United States and that it cannot, therefore, be selling securities, Defendant makes no such claim insofar as its activities in urging the purchase of Bonds are concerned. Clearly, Defendant acts solely for itself, just as any individual might act. In these activities it is not acting as agent or in any other capacity for the Government to any greater extent than any individual interested in the affairs of his mother country would act nor is it acting as agent for its members except insofar as they approve of such activities.

Defendant does contend, however, that its activities on behalf of purchasers of the Bonds are solely the activities that any agent would perform for his principal.

The Commission attempts by indirection to argue that Defendant has caused to be delivered after sale unregistered securities by means of the mails. Defendant has absolutely nothing to do with the delivery of the Bonds after sale. The sale is made in China and the delivery to the purchaser takes place in China at the time of delivery to the purchaser's agent in China. Thereafter the use of the mails is caused by the purchaser's agent. Defendant certainly can have no control over the use of the mails at that time.

The Commission grossly understates the facts in its citation of *Securities and Exchange Commission* v. *Starmont*, 31 F. Supp. 264 (Ed. Wash. N. D., 1940). In addition to the fact that the persons were held to be "issuers", the Court found that the instrument signed by the members of the public in accordance with the so-called "requests" was more than an indication of assent. It was an actual subscription to the stock and hence there was a sale of a security.

Securities and Exchange Commission v. *Torr*, 15 F. Supp. 315 (S. D. N. Y., 1936), 87 F. (2d) 446 (C. C. A. 2, 1937), 22 F. Supp. 602 (S. D. N. Y., 1938), cited by the Commission (B. 9), is clearly not in point because the persons enjoined in that case were clearly acting as agents for those engaged in the sale of the securities.

We have already discussed (supra, 9-10) the opinion of the Commission's General Counsel, referred to by the Commission (B. 10).

We think that far from confusing the facts as contended by the Commission (B. 11), the learned Court below in his opinion (R. 36) demonstrates a complete understanding of the facts.

What we have said in Point I hereof effectively refutes the argument made by the Commission under heading B of Point II of its brief in support of its contention that Defendant is an "underwriter".

The only argument worthy of notice which we have not touched on is the argument that the phrase "for the issuer" should be construed to mean "for the benefit of the issuer". Although the fallacy of this appears on its face, we wish to point out to the Court the highly illogical and strange results which would arise from any such construction.

In this very case, the Commission contends (B. 25-26) that, despite the admitted facts that Defendant is in no contractual, agency or other relationship with the Government, Defendant, nevertheless, can, on behalf of the Government, file a registration statement. The absurdity of this is apparent for not only might the Government be wholly unwilling that a registration statement be filed but the Defendant itself is not in a position to obtain the necessary information required in the registration statement. The Court below recognized this, stating in its opinion (R. 37):

> "Since the defendant is not an underwriter or an agent it has no authority to do so."

The Commission has pointed out (B. 2-3) that the whole purpose of the Statute is to afford "protection to the investing public simply by requiring publicity of the material facts and circumstances concerning securities publicly offered" and that the Commission's "sole function in the registration process is to require that accurate information is made available to persons to whom securities are offered".

The argument of the Commission would lead to the absurd and illogical conclusion that any person could make himself an underwriter for any corporation or government and under the provisions of the Act bind such corporation or such government without the consent, and, in fact, against the wishes, of such corporation or government.

The Commission argues (B. 18) that the principal difference between Defendant's activities and those of an ordinary underwriter is that Defendant's activities "are motivated by patriotism rather than by profit, and its services are contributed voluntarily". *The real difference between*

Defendant and an ordinary underwriter is that the latter is an agent of the issuer. Defendant is not an agent of the Government.

The Commission's argument (B. 19), based on the legislative history of Section 2(11), is not justified by a comparison of the definitions. Such a comparison merely shows an intention that the element of compensation should not be necessary. It does not, however, negative the necessity that there should be an agency relation. This is not only clear from the Act but is conceded by the Commission when it states (B. 19) that the term was meant to include all persons who sell *for an issuer*.

It seems to us also that another reason for the changes made was that the earlier definition might not cover persons who bought an issue of securities and resold such issue for their own account.

In Point II and II-A, the Commission argues that the Act was designed primarily to deal with the problem of "distribution" of securities; that the exemptions set forth in 4(1) were not intended to provide an exemption to any party "engaged in the initial distribution of securities"; that the sale of Bonds by the Government is a "distribution" of securities; that "Defendant is distributing securities; and that defendant's activities are a part of" a transaction by an "issuer" and, accordingly, are not exempt under Section 4(1). It argues that there is a single transaction and that the exemption provided by Section 4(1) does not apply to "component parts" of such transaction.

Although this argument is extremely ingenious, we believe that its fallacy is apparent on its face. The fallacy of the argument is more clearly apparent when we consider the facts. The Government is not violating any law in selling its Bonds in China to the purchaser's agent there. Defendant, in urging others to purchase the Bonds, does not in any way repreesnt the Government. Defendant's action is entirely distinct from the action of individual purchasers in purchasing the Bonds. The latter initiate

such purchases. Defendant's activities are entirely outside the transaction between the Government and the purchasers of Bonds.

Even if this were not true, the Commission attempts by its argument to limit the exemptions which are clearly set forth in Section 4(1). That section provides specifically that transactions by any person other than an "issuer, underwriter or dealer" are exempt. The language is perfectly clear and is not susceptible of any such strained construction as the Commission tries to give it (R. 38).

We do not hesitate to concede that the Courts and the Commission are correct in holding representatives, agents and employees amenable to the Act But in the present case Defendant is not a representative, agent or employee of the Government. The cases cited by the Commission, therefore, have no bearing.

The Commission refers to the fact that it has in certain cases obtained consent injunctions in connection with the sale of the Bonds and makes the statement that the defendants in such cases "were in the same position as the defendant in this case". We are sure that this statement must have been made inadvertently by the Commission because that is not the fact. In all of such cases, it was apparent that there was a certain relationship between the Government's representatives in this country and the persons enjoined from which it could be inferred that the latter were acting as agents of the Government and hence could be held to be "underwriters". We reiterate that in the present case Defendant acts purely voluntarily and has no authority to act for the Government here.

C. Defendant is not "aiding and abetting" a violation of the Securities Act.

In Point III of its brief, the Commission argues that the Defendant should be enjoined as one who is aiding and abetting a violation of the Act. The Commission states (B. 21) "it is clear beyond doubt that the Chinese Government itself is transmitting or causing to be transmitted to

the United States unregistered securities issued by it". Not only is this not clear, but it is entirely contrary to the fact. The Chinese Government sells the Bonds in China to the purchaser's agent in China. After the sale of the Bonds, the Government has no control over the disposition made of the Bonds by the purchaser's agent. In fact, it is immaterial to the Government whether the purchaser allows his agent to retain the Bonds in China or directs his agent to send them to him in the United States.

Furthermore, the Government, on the admitted facts, does not carry on in this country any activities in connection with the sale of the Bonds.

Accordingly, the Government in no way violates the Act. If there is no violation of the Act on the part of the Government, i. e., the principal, then it is clear that the cases cited by the Commission under Point III have no bearing on the case. As a matter of fact, we do not dispute the holdings of those cases.

As we have pointed out, the argument under this point is based on the fallacious assumption that the Government is violating the Act. As we have shown, this is not the case.

D. An injunction against Defendant is not only not the proper remedy but would be highly improper.

In Point IV of its brief, the Commission, referring to a statement made by the learned Court below in its opinion (R. 37), argues that the Act authorizes injunctive relief against Defendant because "it is the agency primarily responsible for the distribution of Chinese bonds in this area" and that recourse to diplomatic channels is not required.

The Commission is clearly in error for two reasons. In the first place, its argument is based upon the assumption, shown to be fallacious, that Defendant is an agent for the distribution of the Bonds. In the second place, if Defendant were an agent of the Chinese Government, it would seem to be obvious that the ordinary rules of International Law as applied by the Courts of this country would be

applied, namely, that injunctive or other relief cannot be granted against a foreign government and that the proper procedure would be as indicated by the learned Court below when it says (R. 37) "the channels of diplomacy are open through the Department of State".

The Commission argues that such procedure is unnecessary because a registration need be signed only by the underwriter of the securities. Since Defendant is not an underwriter of the securities, it is not only not necessary for it to file a registration statement but it "has no authority to do so" (R. 37).

Defendant is not even "acting in a merely ministerial capacity" (B. 26).

POINT III

The judgment of the District Court should be affirmed and the Commission's appeal dismissed.

As demonstrated above, the Commission has failed entirely in its attempt to support its contentions.

Although we have agreed with the Commission that, in urging the purchase of Bonds, Defendant acts purely for itself and represents neither the Government nor the purchasers of Bonds in so doing, the actual fact is that Defendant's activities in this regard merely are the embodiment of the feelings of all of its members. To this extent, therefore, its activities are the activities of its members.

In urging the purchase of Bonds, Defendant is not an agent of the Government. Its activities as agent for purchasers has no bearing on its activities in urging the purchase of Bonds. This, the Commission concedes (B. 11).

Defendant's activities in urging the purchase of Bonds are not a part of any transaction resulting in the purchase of Bonds, any such transaction being one purely between the purchaser and the Government.

Defendant, in urging the purchase of Bonds, is doing no more than what its individual members could do. There is

no rule of law prohibiting an individual from urging someone else to purchase Bonds where he has no interest in the sale of the Bonds except the very human interest of aiding his mother country. As the Court below states in its opinion:

> "The defendant's participation was that of a voluntary charitable organization appealing to the humanitarian instincts and endeavoring to arouse the patriotic fervor of its members, through the medium of newspaper advertisements and mass meetings, to buy bonds of the Chinese Republic and thereby aid their fatherland in its defense in an undeclared war being waged by Japan. The defendant received, and in some instances, assisted in filling out, the subscriptions and delivered them, accompanied by the required funds, to the Bank of China, New York Agency, which accepted and transmitted the subscriptions to and received the bonds from the issuer direct and made the distribution to the purchasers.
>
> "The defendant simply acted for its members more effectively than they might have done for themselves with a saving of their labor and loss of time. Is the defendant more amenable to the provisions of the Act than its individual members for whom it acted?"

We submit that the learned Court below reached the proper conclusion, that its judgment should be in all respects affirmed and the appeal dismissed.

Respectfully submitted,

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