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News

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"Thanks," NASD

SEC reverses trial examiner's findings against member in case involving information disclosure.

"I wish to thank you and the NASD for helping me fight my battle."

The quotation is from a letter a member sent to the Executive Director of the Association after the member had been absolved by the Securities and Exchange Commission of charges of violations of the Securities Exchange Act. NASD intervened in support of the member's defense against the charges.

Proceedings against the member were instituted on allegations that he knew of an offer to be made to stockholders of a certain company to purchase their stock at a price several points above the then-prevailing market. At the time the member, acting as broker, had orders to purchase the stock for a director of the company whose stock was to be bought by another organization. The member did purchase moderate amounts for his customer. The contention of the SEC staff in arguing the case was that the member should have disclosed to sellers of the stock that an offer for the stock was to be made and that the buyer was an "insider" of the company.

The Commission in its decision found that the record did not establish that the member knew of the offer that was to be made to buy the stock he was purchasing for the official of the company. In deciding as it did, the Commission over-ruled its Trial Examiner who found that the member had wilfully violated the Act.

NASD intervened in the case upon learning of the issues involved. The Association took the position, on behalf of its members, that the Commission must reject the finding of the

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**HEALY, McCONNAUGHEY,
CAFFREY, McENTIRE
AND HANRAHAN**

Were the SEC Commissioners partners of a law firm the name of it could be just that—Healy, McConnaughey, Caffrey, McEntire and Hanrahan.

The Commission, as presently constituted, is the result of several changes of very recent origin—principally the resignation of Ganson Purcell, Chairman for four years.

Edmond M. Hanrahan of New York was appointed by President Truman to fill the unexpired term of Mr. Purcell—that is, until June, 1947. Mr. Hanrahan was born in New York August 14, 1905. He attended local schools, graduating from Fordham Law School in 1928. He has acted as counsel to the State Superintendent of Banks.

Richard B. McEntire of Kansas was sworn in as a Commissioner June 4 to succeed Sumner T. Pike, term expiring June 1948.

A few days before his resignation took effect, Mr. Purcell, for the SEC, submitted a report to Congress containing recommendations for amendments to the Securities Exchange Act. Space in this issue does not permit review of all of the SEC recommendations. An early issue will go into them in detail and they will be a subject for thorough discussion by the Board of Governors at its next meeting.

MEMBERSHIP GROWTH

Membership in the Association on June 30 was 2,514, an increase of 47 since March 31 and of 142 for the first six months of 1946. The total on June 30 was the highest since September, 1942.

The Board Meets

Bretton Woods gathering takes up NASD problems. Annual convention suggested.

The Spring Meeting of the Board of Governors and Advisory Council, held June 10-11 at Bretton Woods, New Hampshire, was featured by discussions of a proposed SEC Rule dealing with so-called "free-riding" in new offerings of securities, particularly common stocks, as well as amendments to the Uniform Practice Code to meet new trading and delivery problems, business conduct matters, broadening of quotations sponsored by NASD, and problems concerned with methods of assessment of members.

Articles covering a number of these subjects will be found in this edition of the NEWS. The two-day meeting was attended by 19 of the 21 Governors and 12 of the 14 District Chairmen, who serve as an Advisory Council to the Board. In addition, 6 Chairmen of National Committees attended and submitted reports.

Officers of the Association who attended are:

Wm. K. Barclay, Jr., Chairman, Stein Bros. & Boyce, Philadelphia; Harry W. Beebe, Vice Chairman, Harriman, Ripley & Co., Incorporated, New York; June S. Jones, Vice Chairman, Atkinson, Jones & Co., Portland; John J. Quail, Treasurer, Quail & Co., Davenport; Wallace H. Fulton, Executive Director, Washington.

The following Governors were in attendance:

L. Raymond Billett, Kebbon, McCormick & Co., Chicago; Herbert F. Boynton, H. F. Boynton & Co., Inc., New York; Hermann F. Clarke, Estabrook & Co., Boston; W. Rex Cromwell, Dallas Rupe & Son, Dallas; Irving D. Fish, Smith, Barney & Co., New York; Harlan Herrick, The Lathrop-Hawk-Herrick Company, Wichita;

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The Board Meets

(Continued from preceding page)

Robert C. Kirchofer, Kirchofer & Arnold, Inc., Raleigh; Walter E. Kistner, A. C. Allyn and Company, Chicago; Robert S. Morris, Robert S. Morris & Co., Hartford; Norman Nelson, Piper, Jaffray & Hopwood, Minneapolis; B. Winthrop Pizzini, B. W. Pizzini & Co., Inc., New York; Joseph L. Ryons, Pacific Company of California, Los Angeles; John B. Shober, Woolfolk, Huggins & Shober, New Orleans; J. Robert Shuman, Shuman, Agnew & Co., San Francisco; Burdick Simons, Sidlo, Simons, Roberts & Co., Denver.

Members of the Advisory Council who attended the meeting follow:

Herman L. Lind, Camp & Co., Portland, Ore.; J. Lester Erickson, Wm. R. Staats Co., Los Angeles; J. P. Woollores, Wulff, Hansen & Co., San Francisco; J. Wallace Coxhead, Bosworth, Chanute, Loughridge & Co., Denver; Guy M. Phillips, Caldwell, Phillips Co., St. Paul; Lawrence J. Gable, Taussig, Day & Company, Inc., St. Louis; Sampson Rogers, Jr., McMaster Hutchinson & Co., Chicago; H. Wilson Arnold, Weil & Arnold, New Orleans; Charles H. Pinkerton, Baker, Watts & Co., Baltimore; George L. Morris, Hornblower & Weeks, Philadelphia, T. Jerold Bryce, Clark, Dodge & Co., New York; Carrell K. Pierce, H. M. Payson & Co., Portland, Me.

In addition, the following National Committee Chairmen attended:

Henry G. Riter, 3rd, Public Relations, Riter & Co., New York; Joseph T. Johnson, Special Advisory Committee to Finance Committee, The Milwaukee Company, Milwaukee; George Geyer, Quotations, Geyer & Co., Incorporated, New York; Harold C. Patterson, National Uniform Practice, Auchincloss, Parker & Redpath, Washington; W. Yost Fulton, Special Committee on Research in the Capital and Securities Markets, Maynard H. Murch & Co., Cleveland; R. Victor Mosley, Traders, Stroud & Company, Incorporated, Philadelphia.

In addition to considering the numerous formal subjects on the agenda, the Board heard reports from each Chairman of the 12 District Committees represented at the meeting. Each Chairman gave the Board an informal statement of conditions in his District, of problems of the membership in the District, and of major matters of interest. Recommendations

Announcement

The following advice to members is given upon recommendation of the National Uniform Practice Committee.

TO MEMBERS OF THE ASSOCIATION:

During the past few months there appears to have been a market in certificates of railroad and utility companies which, upon consummation of reorganization, have surrendered their charters and have delivered their assets to successor organizations.

On June 9, 1945, the Securities and Exchange Commission issued Release #3699 (Securities and Exchange Act of 1934) in which it mentioned the fact that certain classes of security holders of the Associated Gas and Electric Company either did not participate, or participated only conditionally in the reorganized company. The release also states "Attention is further directed to the possibility that brokers and dealers who buy or sell Associated Gas and Electric Company or Associated Gas and Electric Corporation securities without adequate disclosure of the status of those securities under the plan may be found to be violating the fraud provisions of the Securities Act of 1933 and the Securities and Exchange Act of 1934."

In the opinion of the Board of Governors, the same principle applies to transactions in certificates of any defunct organization, and members are reminded that failure completely to disclose the status of such certificates at the time of the transaction might involve them in a violation of the Securities Acts mentioned above.

were made by several that meetings be held of members on a District-wide basis, at which opportunity would be had to discuss current problems of the membership. Spokesmen for Districts where meetings attended by the Chairman and Executive Director have been held in recent years advised the meeting that these have contributed progressively to knowledge of Association activities and the relation of these activities to the business of individual members.

The Board also was advised that there is a feeling among the membership in one or more sections of the country that an annual convention of members should be arranged.

"Thanks," NASD

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Examiner that a broker has a duty to state to a selling shareholder the identity of the purchaser because he may be an officer or director of the issuer or otherwise affiliated with it. The Association further argued that a broker cannot be compelled to disclose to sellers the identity of a purchaser or the reasons for his purchases.

The Commission did not pass on the question of whether, had the member known of the impending offer to purchase the stock, he would have violated the Act by not making disclosures of the facts known to him.

"The argument of the staff," said the NASD in a brief, "is based entirely upon the premise that respondent knew or had reason to know of the existence of an offer. . . for the purpose of argument it is here assumed that respondent neither had such knowledge nor had reason to know thereof. The Examiner's report rests upon the premise that a broker buying securities for, or selling securities to a customer, who is an officer or director of the issuer, must disclose the identity of such customer to the dealer selling or purchasing."

Reporting on the outcome of the case to a meeting of the Board of Governors, Wallace H. Fulton, Executive Director, pointed out that because of the private nature of the proceedings NASD did not learn the issues involved until the matter had been set down for argument before the Commission and the Trial Examiner's report had been filed. Mr. Fulton concluded his reference to the case as follows:

"I feel confident that it is the desire of the Board that the Association take a stand beside a member involved in proceedings before the Commission when broad issues of general concern to the membership are involved. In this case a very fundamental question was involved. We are gratified at the result."

Business Conduct

Excessive Mark-ups bring fine of \$1,000, "severe censure", letter of compliance.

A fine totalling \$1,000, as well as "severe censure" was imposed upon a member by a District Business Conduct Committee which found him in violation of Sections 1 and 4 of Article III of the Rules of Fair Practice. The Board of Governors did not call the case up for review, nor did the member disciplined appeal the decision to the Board. In addition to the fine and censure, the District Business Conduct Committee, as part of the penalty, required the member to submit a letter promising compliance with all rules of the Association in the future conduct of his business.

The basis of the complaint was a charge that the member engaged in the practice of selling securities to and buying securities from customers at prices which were not fair, and as examples of this practice, the District Business Conduct Committee cited a number of transactions of the member with customers.

The respondent's initial answer to the complaint was that the Sections of the Rules of Fair Practice alleged to have been violated were invalid and void in that they were unreasonable and arbitrary, indefinite and uncertain, and beyond the power of the Association. The respondent member also denied, in its original answer, having violated the Rules. At the hearing before the District Business Conduct Committee, however, counsel for the respondent admitted the facts as set forth in the complaint, adding that the firm's customers were largely small purchasers of unlisted securities from whom purchases were made by the member at little or no profit. Finally, counsel for the respondent, while acknowledging the seriousness of the infractions charged in the complaint, pledged the firm's full cooperation in close adherence to the Rules of the Association, requesting at the same time that this pledge be considered by the Committee in deciding the complaint.

In its findings, the Committee decided that instances were disclosed where the member involved had realized mark-ups of 10% to 20% above current market prices in transactions where the sale to the customer was made on the same day securities were purchased by the member. The Committee also found that, although a

number of the securities involved were of low price, the dollar volume in the individual transactions amounted to substantial sums. Specifically, the Committee fined the member \$500 for violation of Section 1 and \$500 for violation of Section 4.

District Business Conduct Committees filed seven complaints against members during the first five months of 1946. During the complete year 1945, sixteen complaints were filed.

REPORT ON QUOTATIONS

Governors of the Association, at their last meeting, received and approved a report of George Geyer, Chairman of the National Quotations Committee, describing the growth in number of quotations of over-the-counter securities being published in newspapers and of the increasing number of papers regularly publishing NASD-sponsored quotations.

In view of this trend, Mr. Geyer recommended that District Quotations Committees be expanded and that supervision of quotations be increased and, further, that four regional subcommittees be appointed to function under the National Quotations Committee. Under this latter recommendation, it is contemplated that the regional committees have as their chairmen representatives of the regions now serving on the National Quotations Committee. Mr. Geyer said it was the objective of the National Quotations Committee, through the District Quotations Committees to have newspaper lists carry, in addition to quotations for the day, the comparable bid prices of the preceding day as well as current dividend rates on the issues quoted.

FALL MEETING

Recommendations of Governors representing the Pacific Coast and other western points, as well as past requests of members to the same effect, persuaded the Board of Governors, at its meeting June 11, to vote in favor of holding the Fall Meeting of the Board and Advisory Council at Del Monte, California.

This meeting will be held October 15 and 16. In addition to the 21 Governors, the 14 District Chairmen of the Association also will attend the meeting. It will be the second time since NASD was formed that a meeting of the Governors and Advisory Council has been scheduled west of Chicago.

IBA Program

NASD members invited to participate in educational program.

NASD members are being offered an opportunity to participate in the educational program being conducted by the IBA to attract and train new men in the securities business and to foster wider knowledge of the investment banking and securities business.

The IBA has issued the first of a series of 12 booklets entitled "Fundamentals of Investment Banking," based on courses being conducted in cooperation with Northwestern and New York Universities. These booklets are useful in teaching new personnel the nature of various kinds of securities, corporation practices in the issuing of securities and declaring of dividends, general procedures in the distribution of securities, interpretation of corporation financial statements and their effect on securities prices, appreciation of the needs of individual investors in the selection of securities, and general factors which influence the trend of securities markets. The booklets also contain a list of suggested textbooks.

The 12 booklets are being offered to NASD members at \$35 for the set.

The Board of Governors believes that "Fundamentals of Investment Banking" can be used to advantage by members new in the securities business, by more experienced members in the training of new personnel, and by all members as reference material on basic problems of the business.

Members desiring to subscribe for the series should address inquiries and orders to the Executive Office of the Association.

QUESTIONNAIRE

The Association's Executive Office is completing analyses of questionnaires filed by members during the past two months. The forms are sent to District Committees as the work of listing markets and making computations is finished. Members this year were called upon to report pricing practices in 40 principal transactions.

The registration of new equity securities in the first quarter of 1946, aggregating \$599,217,000, set an eleven-year record for similar periods.

Registered Representatives

Disabilities Shown By Applicants

Under the provisions of Section 2 of Article I of the By-Laws, no member who has associated with him as a principal or employee a person who was the cause of a suspension or expulsion from a stock exchange or NASD, or who was the cause of a suspension or revocation of a registration with the SEC, may be continued in membership except with the approval or at the direction of the SEC.

As a result of adoption by the membership last year of an amendment to the By-Laws providing for registration of "Registered Representatives," nine members have had to be notified that they were in violation of Section 2 of Article I by employing as many applicants for registration as "Registered Representatives." The applications of these individuals disclosed disabilities of the kind defined in Section 2. Members could continue to employ such individuals as "Registered Representatives" only with the approval or at the direction of the SEC.

Four of the members to whom such notices had to be sent have undertaken to have the disabilities of their applicants for registration removed. The procedure followed in such cases is to have a hearing before the District Committee having jurisdiction over the instant member. At such hearings, testimony is taken and evidence presented as to the character, record and qualifications of the applicant for registration, particularly his activities since an action of the kind specified in Section 2 was taken. The District Committee considers the evidence brought out at such hearings and makes recommendations to the Board of Governors, either approving or disapproving admission of the individual to registration. The Board of Governors, upon receiving such recommendations, conducts its own investigation and also may hold hearings. The Board then submits its findings to the SEC. The latter also may hold hearings.

The controlling Section of the By-Laws of the Association is taken almost verbatim from the Securities Exchange Act of 1934—Section 15A (b)(4). The procedure followed, therefore, is specified in the Act.

DEFINITION

"The term 'registered representative' means an officer, partner, employee or other representative of a member engaged in the managing, supervision, solicitation, or handling of listed or unlisted business in securities; or in the trading of listed or unlisted securities; or in the sale of listed or unlisted securities on an agency or principal basis; or engaged in the solicitation of subscriptions to investment advisory or to investment management services furnished on a fee basis. . . ."

If you or one of your associates meets the above qualifications and is not registered with the Association you or such person should apply immediately.

It will be noted that PARTNERS AND OFFICERS are not excluded from the requirement that they register.

Since no member shall permit any person to engage in securities transactions for him unless the person is registered, unregistered partners, officers, salesmen and traders expose a member to charges of violations of Article XV of the Rules of Fair Practice. (See Page B-47 of the MANUAL)

HOW BIG IS IT?

Varying estimates are made from time to time as to the number of securities traded over-the-counter. No two of these estimates seem to agree, despite general unanimity that the total is many times greater than the total for all registered stock exchanges. The most recent attempt to arrive at a closely approximate figure is made by Merrill Lynch, Pierce, Fenner & Beane.

Conceding that nobody knows the market's exact size, the firm says "one clue comes from the National Quotation Bureau whose daily sheets list 25,000 different off-board securities a year. In a single day the Bureau often quotes over 5,000 securities. But the securities listed by the Bureau are only the most active issues. All told an estimated 50,000 different securities are traded off board. This compares with about 3,000 issues listed.

23,374 Registered By June 30

Members of NASD as of June 30 had registered with the Association 23,374 "Registered Representatives."

Expansion of the number of firms in the business and employment of members are mirrored in the registration of 2,023 new "Registered Representatives" since the By-Law establishing this classification became effective last January 15.

Amendments to the By-Laws providing for registration of proprietors, partners, officers, salesmen, traders and other qualifying principals or employees of members were adopted a year ago by vote of the membership. The decision to propose such amendments to members was made by the Board of Governors after a lengthy study of the experience of the Association in applying Rules of Fair Practice.

An applicant for registration agrees, as do members, to abide by the By-Laws and Rules of the Association and regulations and decisions thereunder. A "Registered Representative" therefore is in the same position as a member in respect to duties and obligations under the By-Laws and Rules. For violations of these he may be disciplined the same as any member.

In explaining the objectives of registration at the time the matter was submitted to a vote, an official statement said:

"Why is registration of partners and officers being proposed? To establish individual responsibility of principals of member equal to the responsibility of members themselves. Violations (of the Rules of Fair Practice) by one partner or officer without the knowledge or concurrence of other partners or officers could be disciplined in a manner which would not affect the non-participating partners or officers.

"Why is registration of employees being proposed? Salesmen, traders and other employees of a member exercise a degree of discretion and a certain amount of freedom in the normal course of their activities. In so doing, they should be fully acquainted with the standards of practice and of the obligations to abide by the standards which the members subscribed to in joining the Association.