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NEW YORK STOCK EXCHANGE

ELEVEN WALL STREET

NEW YORK 5, N. Y.

G. KEITH FUNSTON  
PRESIDENT

October 18, 1963

TO: Members and Allied Members

SUBJECT: Stock Exchange Review of SEC Special Study

For the past six months, the Exchange has been engaged in a detailed examination of the several sections of the report of the Securities and Exchange Commission's Special Study of Securities Markets as they have become available. This letter is to bring you up to date on the progress we have made so far in that review.

It is, of course, no surprise to the members and allied members that the Special Study Group found no evidence of "fraudulent activity" involving this Exchange. And while the report is critical of some specific details of Exchange operations, in general it does not challenge in any basic respect the Exchange's stewardship of the marketplace. Significant to the entire securities industry is the strong endorsement of self-regulation which appears conspicuously throughout the report.

A fresh perspective can often be obtained from a study made by people outside the Exchange community. Guided by this realization the Exchange has been carefully sifting the Special Study Group's recommendations as though they had been made by management consultants engaged by us. While we might disagree with the Special Study Group's identification of some questions as "problems" -- and perhaps take issue with the emphasis or tone adopted toward others, and may wonder at some of the report's inconsistencies -- nevertheless, it is important that each suggestion be examined fully and objectively in the light of what is best for investors and the nation's economy. For the objective of the Exchange is, and will always be, to provide the best marketplace possible for the investing public and the nation's economy.

Most of the Special Study Group's 155 recommendations relating to the Exchange Community deal with questions or problems which have been identified and considered before, or which the Exchange has been actively working on. Recommendations concerning floor trading, the specialist, and commission rates reflect areas of concern or debate which have been fully explored in the past. Problems of sales supervision and automation have received priority attention for several years. Energetic action in these areas predates the Special Study's interest by a considerable time.

As a result of the study the Exchange assigned high priority to two problems. The Special Study recommended increased attention to member firms' presentation of their research activities, and the Commission asked the Exchange to assume regulation of the odd-lot differential. The broad supplements to the Exchange rules governing member organizations' communications with the public, which were recently issued, include many of the Study Group's recommendations regarding statements about research. In September the Board agreed in principle to regulate the odd-lot differential.

Most of the Study Group's recommendations regarding the Exchange deal with the operation of the marketplace, a delicate mechanism serving the investment requirements of millions of individuals and institutions in this country and abroad. Our market is a working symbol of the free enterprise system, recognized and respected throughout the free world. But this symbol is also a very practical business entity, capable of dramatic reactions to injudicious tampering.

It is one thing from a theoretical viewpoint to recommend changes in the mechanism -- and quite another matter to integrate such changes into day-to-day operations. Before theories can be activated, they must be thoroughly studied; their value to the public and their appropriateness within the overall economic picture must be assured. It is essential, for example, to maintain the market's liquidity and responsiveness to the national investment climate; and it is equally essential to avoid chipping away at the market's foundations by needlessly restricting the activities of any substantial group of buyers and sellers.

Re: Stock Exchange Review of the SEC Special Study

Thus, the Exchange must not merely study the immediate and obvious implications of each specific SEC recommendation; we must also assess the broader and longer-range impact which each may be expected to have on the overall operation of the marketplace.

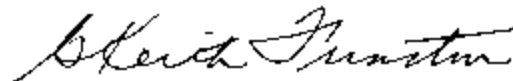
The Board of Governors, of course, will determine Exchange policies and positions, based on its consideration of staff findings, consultants' studies, the Study Group's report and the Board members' own broad experience and knowledge of the securities business. To provide for orderly consideration of each recommendation by the Board, a number of subjects have been assigned priorities, and Special Committees have been established to study the recommendations. A list of these Special Committees and the general area of their specific interest, with some examples of the recommendations, is attached. Copies of the several sections of the SEC Report referred to are, or will soon be, available by writing the Superintendent of Documents, Government Printing Office, Washington, D. C.

The Special Committees are already at work. To assist them and the Board, the Exchange has engaged consultants to study three key areas covered by the Report. An analysis of the cost of handling odd-lot transactions will be conducted by Price Waterhouse & Co., the national accounting firm which devised the Exchange's income and expense reports on member firms' commission business. Cresap, McCormick & Paget, an international management consultant firm, will obtain facts about floor trading. Joel Dean Associates -- a firm of economic consultants headed by Professor Joel Dean of Columbia University -- will examine present and possible future methods of measuring the effectiveness with which Exchange specialists perform their function of endeavoring to maintain orderly markets.

The comments and opinions of the members and allied members will be most helpful and are solicited. They should be sent either direct to a member of the appropriate Special Committee or to the Secretary of the Exchange who will act as a clearing agent.

It is encouraging that SEC Chairman Cary has called for full discussion and study of all recommendations affecting the Exchange. Several meetings have already been held and we are looking forward to future meetings in which Governors and Exchange community experts will participate. We are confident that all of these efforts offer the prospect of continuing progress toward a stronger marketplace, firmly based on the principle and practice of self-regulation and fully responsive to the needs of the investing public.

In addition to the special work involved in considering the SEC Report, the regular work of the Exchange obviously will go forward. As has been our practice in the past, we will continue to search out and adopt improvements in our methods, rules and regulations in all areas whether or not covered by Study Group recommendations.



Attachment

## SPECIAL COMMITTEES

I. Cost & Revenue;    II. Floor Trading;    III. Odd Lots  
IV. Specialists;    V. Steering

### I. Special Committee on Cost & Revenue

#### Members

James F. Burns, Jr. (Chairman)	
Howard E. Buhse (Vice Chairman)	
Harold L. Bache	Robert J. Lewis
Jacob Bleibtreu	Lloyd W. Mason
Louis B. Froelich	Walter Maynard
Frank H. Hunter	Chas. L. Morse, Jr.

1. Split of commissions for non-member broker-dealers - Chapter VI.I (2)
2. Service Charges - Chapter VI.I (4)
3. Procedure for varying the commission rate automatically when volume changes - Chapter VI.I (6)
4. Increase of Floor brokerage on discretionary orders - Chapter VI.D (7)
5. Volume Discount - Chapter VI.I (3)
6. General study of both the rate structure and level of commission rates - Chapter VI.I (5)

### II. Special Committee on Floor Trading

#### Members

Walter N. Frank (Chairman)	
Andrew M. Baird	Gustave L. Levy
James Campbell, Jr.	Joseph A. Meehan
Harold H. Cook	Harry C. Piper, Jr.
Richard M. Crooks	Albert Pratt

1. Abolition of Floor Trading - Chapter VI.F (1)
2. Establishment of "auxiliary specialists" - Chapter VI.F(2)

### III. Special Committee on Odd Lots

#### Members

D. Frederick Barton (Chairman)	
Harold H. Cook	Louis Meyer, Jr.
William J. Denman	C. Peabody Mohun
Benjamin Einhorn	Walter S. Robertson
Louis B. Froelich	Robert L. Stott
Stephen A. Koshland	

1. Cost study of odd-lot business - Chapter VI.E (2)(b)
2. Exchange regulating the odd-lot differential - Chapter VI.E(2)(a)
3. Exchange adopting rules with respect to handling of odd-lot orders and odd-lot dealers offsetting round-lot transactions - Chapter VI.E (3)

(OVER)

4. Disclosure of odd-lot differential in confirmations to customers - Chapter VI.E (6) and VI.I (8)

IV. Special Committee on Specialists

Members

	Henry M. Watts, Jr. (Chairman)
John A. Coleman	John J. Phelan
Richard de La Chapelle	John J. Sullivan
Walter N. Frank	Milton R. Underwood
Robert J. Lewis	Alexander Yearley, IV

1. Increase in specialists' capital requirements - Chapter VI.D(4)
2. Prohibit specialists introducing, carrying or servicing public accounts - Chapter VI.D (7)(f)
3. Prohibit specialists "stopping" stock against an executable order on the book - Chapter VI.D (7)(c)
4. Prohibit specialists' Long Term Investment Accounts and use of Lifo basis - Chapter VI.D (6)
5. Refine the obligations and responsibilities of specialists - Chapter VI.D (2) & (3)
6. Abolition of Specialists-Corporate Liaison Program - Chapter VI.D (Special Item)

V. Special Steering Committee

Members

	Henry M. Watts, Jr. (Chairman)
	Walter N. Frank (Vice Chairman)
D. Frederick Barton	G. Keith Funston
Howard E. Buhse	Frank H. Hunter

1. Possible creation of Associate Memberships - Chapter VI.I(2)
2. Extension of full or partial voting power to Allied Members - Chapter XII.B (2)
3. Increased representation of public brokerage firms (non-specialists) on the Board of Governors, Advisory Committee, Nominating Committee and other governing bodies of the Exchange - Chapter XII.B (2)(b)
4. Limit the Floor Governors' ad hoc powers - Chapter XII.B(3)
5. Publicity by the Exchange (with names) of censures (and fines) given by the Board of Governors or Advisory Committee - Chapter XII.B (6)(b)
6. Examine relationship of Exchange with the S.E.C. and regional Exchanges - Chapter XII.J (1)