

Lafferty, Harwood & Co.
Montreal, Canada

27 February, 1968

The Secretary
Securities and Exchange Commission
500 North Capitol Street
Washington, D.C. 20549

Dear Sir:

We have read through your release No. 8329 dated Friday, January 26th, 1968, and we are naturally aroused by the quality of thinking behind the letter of Mr. Robert W. Haack, President of the New York Stock Exchange.

Not being American citizens or residents of the United States, we do not feel that we should express views with respect to domestic matters. We would, however, like to place on record that we receive give-up commissions from a number of U.S. mutual funds who compensate us in this way for investment research. The economics for maintaining separate research operations covering the Canadian scene cannot be equated with the benefits since the Interest Equalization Tax came into effect, which to a large extent makes the use of Canadian securities prohibitive for investment purposes. On the other hand, the two economies cannot be divorced because they interrelate, and it is very desirable to a research organization in the United States to have effective coverage in this area, and these benefits naturally accrue to the common shareholder.

We have successfully worked in this area to the benefit of the funds and the shareholders, and equally to ourselves because the funds are able to compensate us with give-up commissions. A very recent example is the litigation affecting Texas Gulf Sulphur in Toronto. This trial has been underway for more than 18 months and to date we have published 20 reports covering this litigation with the arguments and testimony from both sides. Some of these reports exceed 150 pages, and obviously they are very time-consuming and expensive to prepare. Had we not undertaken this work and had there not been a basis by which we could be compensated, many of the fund managers in the United States would not have been well informed on what is a very major contingent situation with extensive economic ramifications.

However, this was not the purpose of this letter. Our principal purpose was to contest the views of Mr. Haack, who holds a view that the New York Stock Exchange should be the all-exclusive market, and only members of this

Exchange should have the prerogative of participating in the economic benefits that go serving the investor who trades in these securities.

What Mr. Haack fails to recognize is that it is the smaller investment organizations who act as an effective discipline and restraint on the large New York members who use their tremendous distributing power to create price action on the New York market. It is the smaller groups who act as a deterrent to this by providing a quality of research work which refutes or challenges the type of material often used by the large organizations principally for laying off or distributing institutional blocks of securities to less informed hands.

There is a completely fallacious concept that the quality of investment research lies in the size of the organization. This is not so. The position is actually the reverse. A large organization cannot afford to identify or recognize change without disturbing or antagonizing those groups in whose interests it is desirable a change be not recognized. It is the smaller group who provide the corrective influence to excess prices being stimulated or promoted in the market place.

The attitude of Mr. Haack is completely contrary to the consumer's interest. He seeks to isolate the consumer -- in this case the investor -- from any business exposure, except through those who are members of the New York Stock Exchange. We have had some small minor experiences with the New York Stock Exchange, and it is difficult not to become aroused by the high-handed approach adopted by officials of this Exchange.

We had an incident not too long ago where for some Canadian investors we bought some 10,000 shares of Eurofund Ltd., which is listed on the New York Stock Exchange. The price paid was around 14 1/4. At the time we erred in not recognizing that this stock was subject to the Interest Equalization Tax, and that if our clients were at some stage to divest themselves of these holdings, they would be penalized by having to sell the stock at a substantial discount from the price for these shares on the Stock Exchange. We recognized the error before delivery had been made of the shares, but by this time the shares had moved up to approximately 17 1/4.

We requested that these shares be sold and that we in the meantime would buy the foreign stock, which would avoid the situation. The foreign shares had naturally moved parallel to the domestic shares, and thus we would be buying the foreign stock at a higher price to what we would have bought had we initially purchased the correct shares. The New York member through whom we were working stated that he would have to request New York Stock Exchange permission first to reassign the original contract to his mistake account. This mistake was granted because there was a profit in the transaction. As a result of our error there was a short term profit of some \$3,000 in this transaction, which

we wished to apply for the benefit of our clients to amortize the higher cost that we had to pay on the second round of stock that we purchased because we had not foreseen the tax penalty.

The New York Stock Exchange subsequently ruled that our clients were not entitled to this profit, and the New York member was denied permission to pass this profit to our clients to amortize the higher price for the stock that they later had to pay for. There was no equity in this reasoning at all. The member had contracted to the arrangement, and thus in all legal terms it was a contractual commitment; besides which, the member had been fully paid the commissions to which he was entitled and there was no justification that the fortuitous capital gain which resulted should belong to the member rather than our clients. When we sought equity to this situation with the New York Stock Exchange we might as well have talked to a stone wall. They ruled by divine right and the threat of the stock was their means to enforce the decision on their member.

This kind of attitude and thinking reflects the militancy that exudes through the membership of this organization -- particularly the large national warehouses, who through heavy advertising expenditures seek to create a public image with almost religious tones of purity and divine right.

By broadening the facilities of the regional exchanges, which permits smaller firms such as ourselves to handle business in U.S. securities -- particularly for Canadian investors -- a broader and deeper market is developed, and there is a natural correction to the excess economic power that would otherwise devolve if these opportunities were restricted to members of the New York Stock Exchange where the price admission to the club is now some \$450,000.

We would contend that a great deal less abuse results by broadening the participation in the business than permitting it to concentrate, as would result if the New York Stock Exchange were able to restrict what they term "the leakage of commissions".

It is our understanding that the United States Government is interested in encouraging the participation of non-U.S. residents in the investment of U.S. securities for balance-of-payments purposes. And of course it is the accommodation which has been made to firms like ourselves on the regional exchanges that has contributed to the increased participation in the last two years of Canadian investors in the New York market. Because the capital resources are much more sparsely distributed in Canada, the same economics are not available to support the capital investment costs that are now being capitalized into the privilege of being a member of the New York Stock Exchange. There is, of course, a much higher expense for the broker who is

further away from the center of the market because of the cost and delays in the transshipment of securities and funds to and from that market.

We think it would be directly contrary to the broad public interest, whether the investors be U.S. citizens or those residing outside of the United States, if the New York Stock Exchange were permitted to use the potency of their economic power to restrict the healthy growth and natural development of the regional stock exchanges.

Yours truly,

R. G. D. Lafferty