Eighth Annual Report of the Securities and Exchange Commission

Fiscal Year Ended June 30, 1942

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LETTER OF TRANSMITTAL

SECURITIES AND EXCHANGE COMMISSION,
Philadelphia, Pa.,
June 9, 1943.

Sir:

I have the honor to transmit to you the Eighth Annual Report of & the Securities and Exchange Commission, required by the provisions of Section 23 (b) of the Securities Exchange Act of 1934, approved June 6, 1934, Section 23 of the Public Utility Holding Company Act of 1935, approved August 26, 1935, Section 46 (a) of the Investment Company Act of 1940, approved August 22, 1940 and Section 216 of the Investment Advisers Act of 1940, approved August 22, 1940.

Because of war conditions, we are presenting the report in the most concise and least expensive manner we can devise. The statistical tables have also been substantially abridged. Data in statistical tables customarily shown in previous reports and now omitted are available on request.

In March 1942, the Commission was moved to Philadelphia by direction of the Director of the Bureau of the Budget. It was the Commission’s hope that no issuer who was faced with a deadline in the marketing of securities would be subjected to any delay by the Commission because of the moving. We are happy to report that our hope was realized.

Respectfully.
Ganson Purcell.
Chairman.

THE PRESIDENT OF THE SENATE
THE SPEAKER OF THE HOUSE OF REPRESENTATIVES
Washington, D. C.

SECURITIES AND EXCHANGE COMMISSION
Central Office
18th and Locust Streets

Philadelphia, Pa.

COMMISSIONERS

Ganson Purcell, Chairman
Robert E. Healy
Sumner T. Pike
Edmund Burke, Jr.
Robert H. O'Brien

Orval L. DuBois, Secretary

LOCATION OF REGIONAL OFFICES

Atlanta, Georgia
Palmer Building (Room 415)

Baltimore, Maryland
Baltimore Trust Building (Room 2410)

Boston, Massachusetts
Shawmut Bank Building (Room 426)

Chicago, Illinois
Bankers Building (Room 630)

Cleveland, Ohio
Standard Building (Room 1608)

Denver, Colorado
Midland Savings Building (Room 822)

Fort Worth, Texas
United States Courthouse (Room 103)

New York, New York
Equitable Building (Room 2006)

San Francisco, California
625 Market Street (Room 1501)

Seattle, Washington
1411 Fourth Avenue Building (Room 810)

PART I

ADMINISTRATION OF THE SECURITIES ACT OF 1933

Registration of Securities under the Securities Act of 1933

For information as to the general scope of the registration provisions of the Securities Act of 1933, as amended, the registration and examination procedures, the power of the Commission to institute stop-order proceedings to suspend the effectiveness of the registration statement, and the statutory amendment authorizing the Commission in its discretion to accelerate the effective date of registration statements, reference is made to the Sixth Annual Report of the Commission, the Seventh Annual Report, and previous annual reports.

New Rules, Regulations, and Forms for Registration under the Securities Act of 1933

Further Simplification of Registration Forms. In order further to simplify the registration process, the Commission adopted early in the year two new forms - Form S-2 and Form S-3. Form S-2 is designed primarily for securities of small companies. Form S-3 is available for the registration of shares of mining corporations (other than those in the oil and gas field) in the promotional or the developmental stage. In the case of both forms simplification is secured principally by a provision which permits the prospectus to be filed as the basic part of the registration statement.

Further Simplification of Compliance with Similar Registration Requirements under Different Statutes. The Commission adopted Rule 524 to provide a simplified procedure for registration under the Securities Act of 1933 of securities of open-end management investment companies. The rule provides in effect that any such company may register securities under the Securities Act by filing copies of its registration statement filed under the Investment Company Act, together with copies of a prospectus containing the information given in answer to certain designated items on Form N-8B-1 and certain additional information not required by that form but deemed essential under the Securities Act.

A number of other changes of a minor nature were also made during the year in the rules and regulations governing registration of securities inter the Securities Act.

Disclosures resulting from examination

Through its examination procedure the Commission secured fair and accurate disclosure of material information required in registration statements and prevented the use in many of these documents of information which was misleading and inaccurate. In some instances sales of securities were prohibited by the issuance of stop-orders following formal public hearings.

Statistics of securities registered under Securities Act of 1933

[table omitted]

A total of 755 amendments to registration statements were also filed and examined during the past fiscal year.

Certain registrants under the Securities Act of 1933 also filed during the year, pursuant to Section 15 (d) of the Securities Exchange Act of 1934, a total of 324 annual reports and 137 amendments thereto, all of which required examination.

In addition, the following supplemental prospectus material was filed during the past fiscal year under the Securities Act of 1933:

(1) 180 prospectuses were filed pursuant to Rule 800 (b) which requires the filing of such information within 5 days after the commencement of the public offering;

(2) 230 sets of supplemental prospectus material were filed by registrants to show material changes occurring after the commencement of the offering; and

(3) 315 sets of so-called 13-month prospectuses were flied pursuant to Section 10 (b) (1) of the Act.

Stop Orders, Consent Refusal Orders, And Withdrawal Orders

Withdrawals amounted to 49 during the year and none of the statements involved were refiled to June 30, 1942. Stop orders numbered 7, all of which were still in force at the close of the year. No consent refusal orders were issued during the year.

Securities Effectively Registered

During the fiscal year ended June 30, 1942, securities effectively registered under the Securities Act of 1933 amounted to $2,003,000,000. The issues averaged $7,130,000 in size.

Of all registrations effective during the fiscal year ended June 30, 1942, $476,000,000 were not proposed for sale, $62,000,000 were registered for sale for the account of others than the issuers, and $l,465,000,000 consisted of securities intended to be sold for the account of issuers.

Of the total proposed for sale for the account of issuers manufacturing companies accounted for $468,000,000 or 32 percent, transportation and communication companies $446,000,000 or 30 percent, and electric, gas, and water utilities $389,000,000 or 27 percent.

More than two-thirds of the total value of securities registered for cash sale by issuers or $l,035,000,000 were fixed interest bearing. This included $338,000,000 of secured bonds or 23 percent of the total, and $697,000,000 of unsecured bonds or 48 percent of the total. Common stock amounted to $220,000,000 or 15 percent, followed by preferred stock with $162,000,000 or 11 percent. Certificates of participation, beneficial interest, face-amount installment certificates, etc., added up to $48,000,000 or 3 percent.

A breakdown by methods of issuance showed that $496,000,000 or 34 percent were offered directly by the issuers. Securities offered on an underwritten basis amounted to $899,000,000 or 61 percent and those offered on a best efforts basis aggregated $70,000,000 or 5 percent.

Compensation to he paid to distributors equaled $23,000,000 or 1.6 percent of the gross proceeds of the securities proposed for sale for the account of issuers. Expenses amounted to $8,000,000 or 0.5 percent. The cost of flotation, therefore, was equivalent to 2.1 percent of the gross proceeds. This cost was the lowest for any fiscal year since the series was begun approximately 8 years ago.

Net proceeds, after all issuing and distributing expenses, were estimated at $1,434,000,000. Of these proceeds 51 percent was applied to repayment of indebtedness and 2 percent to retirement of preferred stock. Net proceeds to be used for the purchase of securities were $83,000,000 or 6 percent, including $67,000,000 used for the purchase of securities for investment and $16,000,000 for affiliation. New money purposes accounted for $591,000,000 or 41 percent of the total net proceeds. This included $333,000,000 or 23 percent for plant and equipment and $243,000,000 or 17 percent for working capital. The 41 percent for new money purposes was the greatest proportion of net proceeds for any fiscal year since the Securities Act became effective. The absolute amount intended for new money purposes was the largest amount to be applied from corporate securities to fixed and working capital of any fiscal year since 1937.

Exempt Issues Relating to Oil and Gas Interests

In connection with exempt issues relating to fractional undivided interests in oil or gas rights, covered by Regulation B, there were filed and examined during the year 965 offering sheets, and 876 necessary amendments to such offering sheets, involving securities with an aggregate offering price of approximately $22,177,285.

The following table indicates the action taken with respect to these filings:

Various actions on filings under Regulation B

Temporary Suspension Orders (Rule 340 (a)) -197
(Rule 340 (b)) -1
(Rule 340 (c)) -1

Orders Terminating Proceeding After Amendment -112

Orders Consenting to Withdrawal of Offering Sheet and Terminating Proceeding -55

Orders Terminating Effectiveness of Offering Sheet (No Proceeding Pending) -61

Orders Consenting to Amendment of Offering Sheet (No Proceeding Pending) -597

Orders Consenting to Withdrawal of Offering Sheet (No Proceeding Pending) -104

INVESTIGATIONS OF OIL AND GAS SECURITIES TRANSACTIONS

[table omitted]

Where these investigations show evidence of a violation of the criminal provisions of the Securities Act of 1933, the results are transmitted by the Commission to the Department of Justice, and criminal proceedings are instituted in the discretion of the Attorney General of the United States. In the event such proceedings are instituted, the attorneys and engineers on the Commission staff who participated in the investigation leading up to the proceedings assist the United States Attorneys in the preparation of the cases for presentation to the grand jury and for trial.

Proposed Amendments to the Securities Act of 1933 and the Securities Exchange Act of 1934

During the past fiscal year extensive hearings were held before the Committee on Interstate and Foreign Commerce of the House of Representatives on various proposals to amend the Securities Act of 1933 and the Securities Exchange Act of 1934.

Beginning in July 1940, the Commission and its staff conferred almost continuously with representatives of the securities industry and other interested persons on a large number of proposals to amend various provisions of the 1933 and 1934 Acts. The conferees consisted primarily of representatives of the Investment Bankers Association of America, the National Association of Securities Dealers, Inc,, the New York Curb Exchange and the New York Stock Exchange, although both the Commission's staff and Members of the Commission themselves met also with representatives of the regional exchanges and other interested persons. The purpose of these conferences was to define the areas of agreement and disagreement on the various proposals. A substantial area of agreement was found, although the Commission felt compelled to oppose certain of the securities industry's proposals.

On August 7, 1941, the Commission submitted to the House Committee on Interstate and Foreign Commerce and the Senate Committee on Banking and Currency a 54-page report on the various proposals for amendment of the 1933 and 1934 Acts. On July 30, 1941, a 287-page report had been submitted by the representatives of the four industry groups above named. Beginning on October 28, 1941, the Committee on Interstate and Foreign Commerce of the House of Representatives held hearings on the various proposals of the securities industry and of the Commission. These proposals were embodied in a comparative Committee Print rather than a bill.

The hearings were also concerned with three bills which had been introduced independently of the Commission-industry conferences. H. R. 4344 had been introduced by Representative Wadsworth of New York on April 14, 1941, to amend various provisions of the Securities Act of 1933, the Securities Exchange Act of 1934, the Trust Indenture Act of 1939, the Investment Company Act of 1940 and the Investment Advisers Act of 1940. H. R. 5065 had been introduced by Representative Paddock of Illinois on June 16, 1941, to amend Section 2 (1) of the Securities Act of 1933 in order to exempt from the definition of the term "security" interests in employees' investment plans. H. R. 5832 had been introduced by Representative Oliver of Maine on October 15, 1941, to amend Section 12 (f) of the Securities Exchange Act of 1934 in order to prevent national securities exchanges from extending unlisted trading privileges to any security not listed and registered on a national securities exchange.

These hearings continued until December 5, 1941, and as a result of the declaration of war were interrupted until January 20, 1942. They were concluded on January 27, 1942, and the transcript has been printed in five volumes plus an index volume.

No bills embodying any of the proposals made by the securities industry or the Commission have as yet been introduced, The Commission did not initiate the amendment program, and it confined its proposals very largely to those which it deemed necessary in the light of certain of the proposals of the securities industry. Only a few additional proposals, of a corrective nature, were made by the Commission. None of the Commission's proposals would enlarge the area of the Commission's jurisdiction.

This program constituted one of the Commission's major tasks during the past fiscal year.

PART II

ADMINISTRATION OF THE SECURITIES EXCHANGE ACT OF 1934

Registration of Securities on Exchanges

The general purpose and nature of registration of securities on exchanges and the Commission's procedure in examining applications end reports for compliance with the requirements of Sections 12 and 13 of the Securities Exchange Act of 1934, have been described in the Sixth Annual Report of the Commission, and previous annual reports.

New Rules, Regulations, and Forms For Registration of Securities on Exchanges

Disclosure Contravening Code of Wartime Practices. The Commission adopted Rule X-6 providing for the omission or confidential treatment of any information, filed with the Commission or any securities exchange pursuant to the Securities Exchange Act of 1934, which is inconsistent with the standards of the Code of Wartime Practices promulgated by the United States Office of Censorship. [Footnote: This rule became effective February 19, 1942. At the same time the Commission adopted and made effective companion Rules 171 under the Securities Act of 1933 and U-105 under the Public Utility Holding Company Act of 1935 providing for corresponding wartime censorship of information filed under these additional Acts. Under these three rules procedure has been established whereby the Commission, in cooperation with the Office of Censorship, will upon request render advance, informal opinions in cases where issuers, underwriters,

or other persons are in doubt as to the extent to which, or the manner in which, particular information may be disclosed in a registration statement, prospectus, report, or other document.]

Action under the rule may be taken either on the Commission's own motion or upon application. The Commission makes a preliminary examination of all applications and reports filed under Sections 12 and 13 in order to delete any such confidential information before these documents are made available for public inspection. The securities exchanges cooperate by temporarily withholding from public inspection the copies of these documents filed with them until the Commission's examination has been completed and the exchanges have had an opportunity to delete from the filings such information as is specifically directed or authorized by the Commission. Immediately thereafter these applications and reports are made available for public inspection. [Footnote: During the last three months of the fiscal year approximately 2,700 filings under Sections 12 and 13 were examined under Rule X-6 and made available for public inspection.]

Temporary Exemption of Substituted or Additional Securities. Effective April 14, 1942, the Commission revised its Rule X-12A-5, which provides temporary exemption of certain securities from registration under Section 12 of the Act. [Footnote: In this system of designating rules, "X" indicates that the rule is under the Securities and Exchange Act, the "12A" that it is based on Section 12 (a) of that Act, and the "5" that it is the fifth rule under that Section.] The revision broadens the scope of the rule and sets forth definite bases for termination of the exemption.

Admission to "When Issued" trading of "Reorganization Rails". The Commission adopted, effective September 30, 1941, certain amendments to Regulation X-12D3 relating to registration of unissued securities for "when issued" dealing on national securities exchanges. The amendments, which are principally contained in a new rule designated Rule X-12D3-10, relaxed the provisions of the Commission's "when issued" trading rules insofar as they apply to "reorganization rails," that is, new securities issuable under a Plan of Reorganization for a railroad or other carrier required to make annual reports under Section 20 of the Interstate Commerce Act, as amended. The principal effect of the amendments is to make the new securities issuable under a Plan of Reorganization for a railroad eligible for admission to "when issued" trading as soon as the Plan of Reorganization has been finally confirmed by the court in which the reorganization is pending and the time during which appeals from the order of final confirmation may be taken has elapsed and no such appeal is pending.

Single periodic report of forms adopted for use under Securities Exchange Act and Investment Company Act. As a further step in its program of simplifying filing

requirements, the Commission adopted during the fiscal year a single annual report form and a single quarterly report form to be used by management investment companies under both the Securities Exchange Act of 1934 and the Investment Company Act of 1940.

Statistics of Securities Registered on Exchanges.

Up to and including June 30, 1942, 2,953 issuers had filed a total of 5,555 applications for registration of securities under Section 12 of the Securities Exchange Act of 1934 and a total of 28,705 annual and current reports under Section 13 of that Act. As of June 30, 1942, the registration of the securities of 2,299 of the issuers was in effect, and the registration of the securities of the remaining 654 issuers had ceased to be effective.

The numbers of applications, reports, and amendments filed with the Commission during the past year relating to the listing and registration of securities on national securities exchanges and to the listing of securities on exempted exchanges are as follows:

Number of applications, reports, and amendments relating to the listing and registration of securities on national securities exchanges -Fiscal Year 1942

Applications for registration -160
Applications for "when issued" trading -20
Exemption statements for issued warrants -17
Annual and Current reports -4,562
Amendments to applications, statements and reports --1,487
Annual reports of issuers having securities listed on exempted exchanges --115

Withdrawal or Striking of Securities from Listing and Registration on National Securities Exchanges

During the year ended June 30, 1942, applications by issuers or exchanges involving 33 issues were filed with the Commission for the withdrawal or striking of such issues from listing and registration on national securities exchanges. At the beginning of the year, applications involving 8 issues were pending and decision upon 1 application remained suspended by the Commission. During the year, the Commission granted applications involving 32 issues and denied without prejudice an application involving 1 issue. Applications involving 9 issues were pending as of June 30, 1942.

During the year, registrations on national securities exchanges of the securities of 6 issuers were ordered withdrawn, under Section 19 (a) (2), upon failure to file the annual reports required under Section 13. Proceedings under this Section involving 3 issuers were pending as of June 30, 1942.

During the year, the Commission received from national securities exchanges certifications of removal involving 185 issues stricken from listing and registration because of payment, redemption, or retirement.

Applications for the granting, extension and termination of unlisted trading privileges on National Securities Exchanges

On June 30, 1942, unlisted trading privileges under clause (1) of Section 12 (f) of the Securities Exchange Act of 1934 continued in 1,341 stock and 192 bond issues. This is a reduction of 32 stock and 29 bond issues from the total as of June 30, 1941.

On June 30, 1942, unlisted trading privileges under clauses (2) and (3) of Section 12 (f) existed with respect to 255 stock and 34 bond issues, trading in odd lots only being authorized with respect to 12 of the stock issues. Except for 14 issues subsequently removed, these issues represent the total extension by the Commission of unlisted trading privileges to the national securities exchanges under these two clauses since May 27, 1936, when the clauses became effective.

Since various issues are admitted to unlisted trading privileges on more than one exchange, the authorizations mentioned above involve substantial duplication of issues of securities covered thereby. On June 30, 1942, 1,596 stock and 226 bond trading authorizations were in effect under clauses (1), (2) and (3), covering 1,065 stock and 226 bond issues counting each issue once only. The latter figures include 508 stock and 200 bond issues which are admitted to unlisted trading privileges only; the remaining issues are fully listed and registered (or, in a few cases, temporarily exempted from registration) on national securities exchanges other than those having unlisted trading privileges therein.

During the past fiscal year, 26 applications were filed with the Commission by exchanges seeking a determination that an altered or substituted security was substantially equivalent to a security theretofore admitted to unlisted trading privileges. Of these applications, 22 were granted and 4 were denied.

Toward the end of the past fiscal year the National Association of Securities Dealers, Inc. intervened in opposition to applications of the New York Curb Exchange for the extension of unlisted trading privileges in 3 bond issues

pursuant to clause (3) of Section 12 (f) and in 1 stock issue pursuant to clause (2) thereof. The matter had not been disposed of by the end of the year.

The number of exempted exchanges permitting unlisted trading in securities remained at four, and the totals of stock and bond issues admitted to unlisted trading thereon were 75 and 4, respectively, on June 30, 1942. Two of the five stock issues admitted to unlisted trading on the Wheeling Stock Exchange under Clause 2 of Section 12 (f) during the 1940 fiscal year were removed in 1941, by reason of exchange into another stock.

Amendment of Rule X-12F-5

Rule X-12F-5 was amended during the year to provide that transactions in listed and unlisted securities may be differentiated either by adding the letter “L” to ticker reports of quotations or transactions in listed securities or by adding the letter “U” to ticker reports of quotations or transactions in securities admitted to unlisted trading privileges.

Special offering plans

During the fiscal year, three national securities exchanges adopted plans which permit special offerings of blocks of certain securities to be effected on their respective floors, These plans provide that a special offering may be made when it is determined that the auction market on the floor of the exchange cannot absorb a particular block of a security within a reasonable time and at a reasonable price. The plans permit a person making such an offering to pay a special commission to the brokers of the purchasing customers and stipulate also that such brokers shall not receive any compensation from their own customers. Provision also is made far the appropriate designation on the exchange ticker tape of transactions effected as part of a special offering and for appropriate confirmations to customers, describing the special character of the transaction.

In order to permit such plans to be instituted on an experimental basis, the Commission, following conferences between its staff and brokers and exchange officials, amended its Rule X-10B-2, which in general prohibits any person engaged in distributing a security from compensating any other person for soliciting or inducing a third person to buy on an exchange the distributed security or any other security of the same issuer. The effect of the amendment, adopted February 6, 1942, is to exempt from the restrictions of the rule transactions which are effected pursuant to a special offering plan which has been declared effective by the Commission. The exemption, however, was declared to be only temporary, to expire on July 31, 1942. [Footnote: On July 8,

1942, the exemption was extended to January 31, 1943. (Securities Exchange Act Release No. 3270).]

Pursuant to the terms of this exemption, the Commission declared effective, as of February 14, 1942, a plan submitted by the New York Stock Exchange. Similar action we taken with respect to a plan of the San Francisco Stock Exchange (effective April 17, 1942), and with respect to a plan of the New York Curb Exchange (effective May 15, 1942). Various modifications in the terms of these three plans have also been declared effective by the Commission. Moreover, on April 16, 1942, the Commission broadened the exemption to Rule X-10B-2 to include special offerings in certain issues having unlisted trading privileges, provided that information is available with respect to such securities approximating that available for listed securities.

In the last four and one-half months of the fiscal year, during which tine the plan was operative, 19 special offerings were made at the New York Stock Exchange. Neither the New York Curb Exchange nor the San Francisco Stock Exchange had announced any special offering by the close of the fiscal year.

Aids to bookkeeping standards

During the past year the Commission staff prepared a series of fifteen forms on which the information necessary to comply with the requirements of Rule X-17A-3 (a) could be conveniently recorded. Such forms were furnished to all regional offices for distribution among brokers and dealers. The use of the forms is optional. They represent a conveniently uniform manner of recording information required to be kept by the rule.

Study of the Regional Exchanges

As a part of a general study of current developments in the securities markets, and at the request of officials of various regional exchanges, representatives of the Commission during the fiscal year undertook field studies of the problems of the regional exchanges. By the close of the fiscal year, Commission representatives had visited Boston, Chicago, Cleveland, Detroit, Los Angeles, Pittsburgh, Salt Lake City, San Francisco, Seattle, and Spokane, to investigate the problems of the exchanges located in those cities. The study had not been completed at the close of the year.

Study of over-the-counter markets in exchange stocks

A study of the characteristics of over-the-counter transactions in exchange stocks, which was begun in the preceding fiscal year, was continued throughout

the past year. One phase of the study was completed during the year and the results were published on February 5, 1942, under the title “Report to the Commission by the Trading and Exchange Division on Secondary Distributions of Exchange Stocks”. This report dealt with the nature, development, and magnitude of over-the-counter offerings of outstanding blocks of exchange stocks.

Substantial progress also was made in the second major phase of this study, dealing with over-the-counter transactions in exchange stocks other than secondary distributions. Approximately 250,000 transactions, representing every such over-the-counter transaction in every exchange stock reported by 4,700 brokers and dealers in the six months ending February 28, 1941 were tabulated in various ways and subjected to a number of different analyses. At the end of the fiscal year, however, the results were not yet in form for public release.

Saving study

The Commission on April 15, 1942, inaugurated a series of quarterly releases on the volume and composition of saving by individuals in the United States. These releases show the aggregate volume of individuals’ savings i.e., the increase in their assets less the increase in their liabilities, exclusive of gains or losses from revaluation of assets; they show also the components contributing to this total, such as bank balances and currency holdings, insurance, securities, consumers’ indebtedness, and consumers’ durable goods. Estimates of business or government saving are not included.

Rule for additional protection to investors

During the fiscal year the Commission adopted Rule X-10B-5 as an additional protection to investors. The new rule prohibits fraud by any person in connection with the purchase of securities, while the previously existing rules against fraud in the purchase of securities applied only to brokers and dealers.

Market surveillance and trading investigations

The Commission’s aim in its administration of the statutory prohibitions of the Securities Exchange Act of 1934 against stock market manipulation is a sufficient policing of the markets in order to accomplish the extinction of manipulation without interfering with the legitimate functioning of those markets. Its methods of market surveillance and its investigatory procedure are set forth at pages 91 et seq of the Sixth Annual Report of this Commission.

[table omitted]

During the fiscal year ended June 30, 1942, the Commission continued the administration of (a) Rule X-17A-2, which requires the filing of detailed reports of all transactions incident to offerings in respect of which a registration statement has been filed under the Securities Act of 1933 where any stabilizing operation is undertaken to facilitate the offering; and (b) Regulation X-9A6-l, governing stabilizing transactions in securities registered on national securities exchanges effected to facilitate offerings of securities so registered in which the offering prices are represented to be “at the market” or at prices related to market prices.

Out of a total of 235 registration statements filed under the Securities Act of 1933 during the past fiscal year, 129 contained a statement of intention to stabilize to facilitate the offerings covered by such registration statements. Because of the fact that a registration statement in some cases covers more than one offering, there were a total of 148 offerings of securities in respect of which the statement required by Rule 827 of the Rules and Regulations under the Securities Act of 1933 was made to the effect that a stabilizing operation was intended to be undertaken. Stabilizing operations were actually conducted to facilitate 91 of these offerings. In the case of bonds, public offerings of $311,192,300 principal amount were stabilized. Offerings of stock issues aggregating 8,729,964 shares and having an aggregate estimated public offering price of $288,356,806 were also stabilized. Of the 91 stabilizing operations commenced during the past fiscal year, 80 had been completed and notices of termination of stabilization filed with the Commission and the remaining 11 were still in progress as of the close of the fiscal year.

Also during the past fiscal year, 5 notices of intention to stabilize were filed with the Commission on Form X-9A6-1 pursuant to the provisions of Rule X-9A6-3. The offerings described in these notices, to facilitate which stabilizing operations were conducted, involved one offering of bonds of $2,470,000 principal amount, and stock issues aggregating 211,900 shares and having an aggregate initial public offering price of $8,310,675.

With a view toward simplifying the procedure for the reporting of transactions effected by persons engaged in stabilizing activities the Commission adopted on July 29, 1941 a new Form X-17A-1, with instructions therefor. This new form was designed to be “self- proving” and to replace the three forms required to be filed by those persons subject to the provisions of Rule X-17A-2 or Regulation X-9A6-1. An amendment to Rule X-17A-2, under the Securities Exchange Act of 1934, required by the adoption of the new form, was also adopted on that date.

To simplify further the filing of stabilizing reports, the Commission adopted on February 13, 1942 an amendment to Rule X-17A-2, eliminating the necessity of filing reports in triplicate and making it unnecessary, in most cases, for a stabilizer to file a report for any day on which his transactions are confined to

retail sales of the offered security at the fixed public offering price. Certain other minor changes were made in the rule for clarification. The instructions for Form X-17A-l were also revised to conform to the amendment to the rule.

Proceedings under Section 19 (b) with respect to the multiple trading rule of The New York Stock Exchange

The Commission's first proceeding under Section 19 (b) of the Securities Exchange Act of 1934, which section empowers the Commission under certain conditions to alter or supplement the rules of an exchange in respect of certain matters if the exchange itself refuses to make such changes, was closed by an order of the Commission. [Footnote: Securities Exchange Act Release No, 3053. See also Securities Exchange Act Release No. 3033. Section 8 of Article XIV (formerly Article XVI) was amended by the New York Stock Exchange to contain the required proviso, effective October 6, 1941.] This order which was entered after extended hearings and argument required that Section 8 of Article XIV (formerly Article XVI) of the Constitution of the New York Stock Exchange be amended to contain the following proviso:

" * * * nothing herein contained shall be construed to prohibit any member, allied member or member firm front, or to penalize any such firm for, acting as an odd-lot dealer or specialist or otherwise publicly dealing for his or its own account (directly or indirectly through a joint account or other arrangement) on another exchange located outside the City of New York (of which such member, allied member or member firm is a member) in Securities listed or traded on such other exchange."

No appeal was taken by the Exchange from the order of the Commission. Many of the smaller exchanges had protested vigorously against the rule as it stood and was interpreted by the Exchange prior to the ordered amendment.

Exchanges Registered and Exempted from Registration

During the past fiscal year there was no change in the number of exchanges registered with the Commission as national securities exchanges, nor did any change occur in the number of exchanges exempted from such registration.

OVER-THE-COUNTER MARKETS

Commission Supervision of Over-The-Counter Brokers and Dealers

In the year ended June 30, 1942 the Commission received from its regional offices, 1,054 reports of inspections of registered brokers and dealers. These

inspections are based on examination of books and records only and are designed to test compliance with the statutes sand rules and regulations thereunder. Prominent points covered are best illustrated by a brief summary of the findings of these inspections. In 368 inspections there were found irregularities which may be classified as follows: 112 instances of unsatisfactory or precarious financial condition; 65 instances of improper use of customers' funds or securities (only 18 of which involved firms whose financial condition was not unsatisfactory); 161 instances of transactions at prices which tended to indicate that sales had been made to customers at prices not reasonably related to the current market; and 28 instances of secret profits, involving misrepresentations as to the prices at which customers' orders had been executed. In many other cases involving the sale of oil royalty interests it was found that sales to customers were at prices grossly in excess of the cost to the dealer.

Administrative Remedies

Public interest and protection of customers are factors which the Commission must weigh and consider prior to the application of a statutory remedy upon consideration of irregularities of the sort described above. In the course of our examination of the books of registered brokers and dealers cases are frequently encountered involving unsatisfactory financial condition or improper hypothecation of customers' securities, in many cases, circumstances suggest that the violations are unintentional. The inspection program being, in part, educational, it has been the Commission's policy, before considering statutory remedies, to give opportunity to firms to correct such conditions. In one case a firm had improperly pledged customers' fully paid for securities but officers who were also principal stockholders disclaimed knowledge of the situation and promptly contributed more than $40,000 to the corporation, discharged responsible employees and reorganized the business. Subsequent surveillance failed to disclose further irregularities by the firm.

In the case of Ver Hulst & Co,, Inc. of Denver, Colorado (Securities Exchange Act Release No. 3204), the Commission, on information tending to show insolvency and improper use of customers' securities, instituted proceedings in February, 1942 to determine whether the firm's registration should be revoked and whether it should be suspended or expelled from membership in the N.A.S.D. Subsequently the firm required withdrawal of its registration, representing that it had paid or arranged to pay $55,000 satisfying an creditors and protecting customers from the possibility of loss, that it was in the process of going out of business and contemplated dissolution, that it had resigned from the N.A.S.D., and that the registrant's President, George M. Ver Hulst, would not again enter the securities business. Under these circumstances the Commission found that withdrawal would not be inconsistent with the public interest and the

protection of investors and ordered, on April 22, 1942, that the withdrawal application be permitted to become effective.

In the case of Morrison Bond Co., Ltd., of Long Beach, California (Securities Exchange Act Release No. 3189), a similar proceeding was instituted by the Commission on information that the company had filed a petition under Chapter XI of the Bankruptcy Act to effect an arrangement with unsecured creditors. The company proposed to continue its broker-dealer business. On April 8 registration was revoked and the firm was expelled from the N.A.S.D. on findings of misleading representations and fraudulent omissions of material facts in the sale of securities, willful violations of the hypothecation rules and alterations and false entries in its books and records. It was stated in the Commission's opinion that the Commission was convinced that the false entries had been made "to avoid discovery of the fact that it (the firm) has violated the Commission's hypothecation rule."

As a result of information obtained in some inspections, civil suits were filed and permanent injunctions obtained, the defendants consenting, against Kimball, Ware & Co., Portland, Maine, Seybolt & Seybolt, Inc., Springfield, Ma., John M. Wyatt & Co., El Paso, Texas, and Hartmann Inc., Wheeling, W. Va. In twelve instances facts relating to serious financial condition were referred to the Attorney General of the State of New York who, after independent inquiry, obtained injunctions against nine of the firms involved. One injunction was later vacated. The capital position of each of the three remaining firms was adjusted and no action against them was taken.

The most difficult current problem arising out of regulation of over-the-counter brokers and dealers stems from the practice of selling securities at prices which bear no reasonable relationship to current market. [Footnote: In July 1942 the Trading and Exchange Division offered to the industry for comment a proposed rule which would require the disclosure to the customer of the best available market for a security before the completion of a transaction in that security.] In such cases extensive investigations beyond the limits of books and records must be made. These investigations tax to the utmost the limited staff of the Commission now available for such work. They require the compilation of voluminous price schedules and the reconstruction of market prices at the time the transactions took place. Customers must be interviewed to determine what representations were made to induce the transactions and whether material facts were concealed from them. In a number of investigations made during the past year the evidence disclosed a pattern of fraudulent conduct which resulted in the formal proceedings. The chief remedy employed in such cases is the revocation of the firm's registration, coupled with expulsion from the NASD, where the firm is a member of that Association.

In ten of the cases decided during the year revocation of registration was ordered because of fraudulent over-reaching of the character just described. Seven of these firms were also expelled from membership in the NASD. Of the ten cases referred to above, two involved not only the sales of securities at prices inconsistent with prevailing market prices but also gross abuse of a relationship of trust and confidence which the firms had established with their customers. Both cases are of importance on the question of agency.

In its findings and opinion in the Allender case, the Commission discussed the legal principle that words alone on a "confirmation" to a customer do not establish the relationship between the parties and held that "the words 'we have this day sold to you' and 'bought from you' do not of themselves contravene the existence of an agency relationship between the respondent and its customers and do not justify respondent's failure to disclose its secret profits." The complete reliance of the customers on the firm's advise, the unequal circumstances of the parties in the transaction, and complete trust and confidence in the firm were held to impose upon it the duty to make full and complete disclosure of all material facts

In the Stelmack case the evidence showed that the firms obtained lists of holdings from certain customers and then sent to these customers analyses of their securities with recommendations listing securities to be retained, to be disposed of, and to be acquired. The firm's order blanks, which customers signed, stated "I hereby authorize you as my agent, for my account and risk . . . to sell . . . buy," but also contained language which authorized the firm, as principal, to "buy from or sell to me . . . at prices to be fixed by you and I hereby ratify and confirm any transaction effected by you pursuant hereto." The Commission held that the conduct of the customers in soliciting the advice of the firm, their obvious expectation that it would act in their best interests, their reliance on its recommendations, and the conduct of the firm in making its advice and services available to them and in soliciting their confidence, pointed strongly to an agency relationship and that the very function of furnishing investment counsel constitutes a fiduciary function. As to the order form, the Commission held that where the language of a document or a course of conduct thereunder create an agency, other provisions in the document explicitly negating the existence of an agency are of no effect.

The Stelmack case in important in another respect. One of the admitted charges which the Commission found to be in violation of the fraud provisions of the Securities Act and the Securities Exchange Act was that, while the corporation was engaged in selling its own preferred stock, it failed to disclose to the purchasers thereof that it had submitted false and misleading financial reports to the Office of the Attorney General in that State which in effect permitted the registrant to remain in business only at the peril of discovery by the Attorney General.

Rules

To facilitate sales of federal stamps and bonds and tax saving notes, registered brokers and dealers and members of exchanges were no longer required to keep records or send written confirmations thereon by amendments to Rules X-17A-3 and X-15C1-4 effective January 21, 1942.

Rules X-15B-8 promulgated and effective June 9, 1942 provides that withdrawal of registration of a broker or dealer becomes effective on the thirtieth day after the filing of a notice, unless prior to its effective date the Commission has instituted a proceeding to revoke or suspend registration or to impose terms and conditions on such withdrawal. If the Commission institutes such proceeding, or if a notice of withdrawal is filed after the Commission has ordered proceedings to revoke or suspend registration, the withdrawal, during the pendency of such proceedings, becomes effective only at such time and on such conditions as the Commission may appropriately order.

The following table contains statistics relating to administrative proceedings under Section 15 (b) of the Securities Exchange Act, which Section governs registration of brokers and dealers:

Revocation proceedings pending July 1, 1941: 11

Denial proceedings pending July 1, 1941: 3

Revocation proceedings ordered during year: 39

Denial proceedings ordered during year: 6

Total: 59

Revocation proceedings dismissed on withdrawal: 4

Revocation proceedings dismissed and not revoked: 2

Denial proceedings dismissed on withdrawal: 5

Denial proceedings dismissed and registration permitted: 1

Registration denied: 2

Registration revoked: 29

Revocation pending, June 30, 1942: 15

Denial pending, June 30, 1942: 1

Total: 59

Registrations

The Commission's experience during the year ended, June 30, 1942 with broker-dealer registrations is shown in the tabulations accompanying this report. Briefly, there was a net decline of 508 registrants to 5,557 as of the end of the period, it is clear that the war effort is a basic cause of at least part of this shrinkage.

The National Association of Securities Dealers, Inc.

The Commission's efforts in regulating the over-the-counter industry have been aided by the cooperation of National Association of Securities Dealers, Inc. (NASD) pursuant to Section 15a of the Securities Exchange Act of 1934, otherwise known as the Maloney Act. During the year under review NASD continued as the only national securities association registered as such with the Commission.

Due largely to diversion of personnel of its membership into war activities, membership in that Association suffered a 12.8% decline from 2,974 members as of July 1, 1941 to 2,593 as of June 30, 1942.

Examination program

As of June 30, 1942 the Association had completed, largely through questionnaires, its initial examination of more than 2,200 members. Less than 700 members then remained uninspected. These examinations, conducted by each of the fourteen District Business Conduct Committees, under the general supervision of the main office of the Association, delve into the business practices of members with emphasis upon the compliance with the Rules of Fair Practice. Reports of examination which indicate violations of the Association's rules result in the filing of either formal or informal complaints by the appropriate District Business Conduct Committee. The scope and results of these disciplinary actions are discussed subsequently.

Cases referred by the Commission to the NASD

The Association's examination program outlined above is not the only source of disciplinary action against members. The Commission, as a matter of policy, frequently refers to the Association information uncovered in its own inspection

which appears to concern either unfair prices or other violations of the Association's rules.

On July 1, 1941 there were before the Association 11 cases which had previously been referred to it by the Commission and, in the ensuing year, 46 other cases were referred. In that time the Association disposed of 46 cases and it held pending 11 cases on June 30, 1942. Of the cases disposed of 23 were handled informally and in the remaining cases 23 formal complaints were filed which resulted in five expulsions, two suspensions, three fines and censures, six fines, four censures, and no action or penalty in three instances.

Disciplinary proceedings by NASD

In disciplinary matters, minor or technical infractions of the Association's rules are generally handled informally and usually result in no more than a formal censure, but in more serious matters formal complaints are filed by the Association which may have as their consequence expulsion, suspension, fine or censure or any combination of those penalties.

On July 1, 1941 there were pending before the Association 19 formal complaints and 332 additional complaints were filed in the following year. Of these 151 cases, 130 were. disposed of in the year and 2l remained in process on June 30, 1942.

Formal complaints were withdrawn or dismissed without penalty in 25 instances; 32 respondents were censured; 47 were fined, in amounts ranging from $25 to $2,000; 12 were suspended for periods of from thirty days to one year; and 24 respondents were expelled. Cases referred by the Commission are included in this summary.

In 20 cases decisions of District Business Conduct Committees came before the Board of Governors for review. The Board affirmed three decisions; dismissed one complaint in which a Business Conduct Committee had censured and imposed a $250 fine; modified a decision of suspension, censure and $1500 fine to censure and $300 fine; and modified a decision of "strong censure" and $100 fine to eliminate the censure. One appeal for review was withdrawn and 12 cases were pending June 30, 1942.

A District Business Conduct Committee decision of censure and $250 fine, affirmed by the Board of Governors was brought by the respondent to the Commission for review but by June 30, 1942 no action had been taken.

Amendments to Rules

Uniform Practice Code. The Commission not disapproving, a Uniform Practice Code covering “Settlement of Contracts and Trading Practice in Over-the-Counter Transactions in Securities” became effective August 1, 1941 after membership approval. This code is technical in substance and codifies on a national scale what was generally recognized as sound practice in the securities business.

Amendments to By-Laws and Rules of Fair Practice. On June 15, 1942 the Association forwarded to the membership for approval or disapproval an elaborate revision of the By-Laws and Rules of Fair Practice after the Board of Governors on May 18 and 19, 1942 had recommended its adoption. Many of the proposed changes only eliminated from the rules of the Association reference to a predecessor organization or material which was of value only in the original organization and registration of the Association. Other changes involved language or detail in which some ambiguity existed or in which experience indicated the necessity for alteration to make the material consistent with the statutes or rules the Commission.

Of paramount importance was an amendment which would require, as a condition to membership, minimum net capital, exclusive of fixed assets of $5000 for “clearing firms” or $2500 for “non-clearing firms.” [Footnote: Balloting, which resulted in membership approval of these changes, was completed on July 15, 1942. Subsequently, in Securities Exchange Act Release No. 3322, the Commission, after extensive hearings and argument, disapproved the minimum net capital requirement.] Other changes included authority to assess a disciplined member some part of the cost of the proceedings in which he was involved and a requirement that members should diligently supervise the activities of salesmen.

The following tabulation relates to broker-dealer registration under Section 15 (b) of the Securities Exchange Act:

July 1, 1941 - June 30, 1942

Effective registrations at close of preceding fiscal year: 6,065

Applications pending at close of preceding fiscal year: 37

Applications filed during fiscal year: 572

Total: 6,674

Applications withdrawn during year: 18

Registrations withdrawn during year: 919

Registrations canceled during year: 97

Registrations denied during year: 2

Registrations suspended during year: 2

Registrations revoked during year: 29

Registrations made inactive during year: 11 [Footnote: The registration of 11 brokers and dealers, whose whereabouts, despite careful inquiry, could not he ascertained, have been placed on inactive status.]

Registrations effective at end of year (except those put on inactive status as explained in footnote above): 5,557

Applications pending at end of year: 39

Total: 6,674

PART III

ADMINISTRATION OF THE PUBLIC UTILITY HOLDING COMPANY ACT OF 1935

Integration and Corporate Simplification of Public Utility Holding Company Systems

In the past fiscal year, the major activities of the Commission in its administration of the Public Utility Holding Company Act of 1935 revolved around the enforcement of the integration and simplification provisions of the Act. In several important cases we have entered orders prescribing most of the action which must be taken ultimately to comply with the requirements of Section 11, particularly Section 11 (b) (1). As to the remaining cases, a majority of the proceedings have reached the stage where such orders may be expected in the near future. In the course of these proceedings the Commission has had occasion to pass upon many of the disputed questions of interpretation of the Act, and the managements of most of the holding company systems are now either substantially advised as to, or in a position to judge the scope of, the action which we will order to be taken to bring about compliance with Section 11. A number of companies have appealed our orders to the courts and the cases now

pending in the courts should settle most of the legal questions still in dispute. We are therefore moving toward completion of the first stage of entering orders and getting the legal formalities behind us, especially with respect to procedure and interpretation. When that stage is completed with respect to the various holding company systems, each will know definitely where it stands in relation to the requirements of Section 11. How and when such orders shall be enforced, is a matter for future determination in most of the cases.

We have not proceeded as yet under Section 11 (d) for enforcement of our Section 11 (b) orders by the courts. A significant result of the progress that we have made in nearing the completion of the first stage of the administration of Section 11 is that many of the major systems have now evidenced a willingness to proceed with the task of carrying out our orders. To that end several of the systems have filed voluntary plans and others are engaged in doing so and in discussing their proposals with us. In fact, with few exceptions we are finding an increasing tendency on the part of the holding company systems to facilitate either the entering of orders, or trial of cases instituted by us, or compliance with the Act. In view of the progress already made, or in prospect, the Commission's major administrative concern today relates to the final steps in achieving the objectives of the statute, namely, the choice between the various alternative methods available under the Act for bringing about compliance with the requirements of Section 11 (b), and the determination that treatment of the various claims of security holders is fair and equitable.

During the 1942 fiscal year, the Commission instituted 26 new proceedings looking to orders requiring registered public utility holding companies to comply with Section 11 of the Act and at the close of the fiscal year, 48 such proceedings were pending. These 48 proceedings involve substantially all of the public utility holding company systems registered under the Act although they do not encompass all of the Section 11 problems existing in such systems. In this connection, it may be noted that as of June 30, 1942, there were registered with the Commission 134 public utility holding companies, the total consolidated book assets of which amount to approximately $16,000,000,000, or about 68 percent of the private electric and gas utility industry of the United States. Those 134 registered holding companies constitute 53 public utility holding company systems, which include 1,342 holding, subholding and operating companies. However, about 14 of them control total consolidated assets of $12,195,000,000 and approximately 52% of the privately owned electric generating capacity of the country. The holding company systems involved in Section 11 proceedings as of June 30, 1942 had consolidated assets which aggregated $14,237,000,000.

Section 11 (b) (1) -- Geographic simplification

The past fiscal year has seen rapid strides toward ultimate compliance by all holding company systems with the geographic integration provisions of the Act. As related in last year's annual report, the previous year was chiefly noted for the holding of public hearings as to the major holding company systems and the entry of initial orders as to acme of them. At the close of that year, however, the records in most of those proceedings had not been completed, and there remained to be instituted additional proceedings as to several systems constituting a minor portion of the industry subject to the Act.

The more significant developments in the administration of Section 11 (b) (1) of the Act in the past fiscal year may be summarized as follows:

(1) Hearings were completed in most of the integration proceedings instituted prior thereto and substantially completed in all others, including a number begun during the year. The Section 11 (b) (1) records were completed with respect to the following systems: Cities Service Power & Light Company, Consolidated Electric and Gas Company, Engineers Public Service Company, Great Lakes Utilities Company, Lone Star Gas Corporation, The Middle West Corporation, North American Gas and Electric Company, Southern Union Gas Company, Standard Gas and Electric Company, United Public Utilities Corporation and Utilities Stock & Bond Corporation. The record in the Associated Gas and Electric Corporation proceeding was completed on substantially all of the issues.

(2) Important, far-reaching orders were entered by the Commission prescribing most of the steps which certain of the major systems must take to comply with Section 11 (b) (1). Attention is directed to the Commission's orders in the following cases:

Engineers Public Service Company -- Holding Company Act Release Nos. 2897, 3230

The North American Company -- Holding Company Act Release No. 3405

Standard Gas and Electric Company -- Holding Company Act Release No. 2929

The United Gas Improvement Company -- Holding Company Act Release Nos. 2913, 3511

The United Light and Power Company -- Holding Company Act Release Nos. 2923, 3189, 3242

United Public Utilities Corporation -- Holding Company Act Release No. 3368

(3) Two of the largest holding company systems, The United Gas Improvement Company and The North American Company, filed petitions to review the Commission's orders in United States Circuit Court of Appeals. [Footnote: On December 24, 1942; without waiting for a decision on its appeal, U.G.I. filed a plan for the divestment of its principal assets (consisting of common stock of Philadelphia Electric Company and Public Service Corporation of New Jersey) by a distribution of such assets among its stockholders. We approved the plan on March 18, 1943 (Holding Company Act Release No. 4173). A petition for review of our order of approval has been filed by stockholders of U.G.I. Our order in the North American case was affirmed by the U.S. Circuit Court of Appeals, Second Circuit, January 12, 1943; 133F. (2d) 148.]

(4) Proceedings were instituted with respect to most of the holding company systems as to which Section 11 (b) (1) cases were not already pending. The new proceedings included the following :

Associated Gas and Electric Corporation -- Holding Company Act Release No. 2983

Consolidated Electric and Gas Company -- Holding Company Act Release No. 3225

Great Lakes Utilities Company -- Holding Company Act Release No. 3243

Lone Star Gas Corporation -- Holding Company Act Release No. 3370

Republic Service Corporation -- Holding Company Act Release No. 3514

Southern Union Gas Company -- Holding Company Act Release No. 3586

United Public Utilities Corporation -- Holding Company Act Release No. 3105

Utilities Stock & Bond Corporation -- Holding Company Act Release No. 3566

(5) A number of important interpretations of the provisions of Section 11 (b) (1), together with determinations of general policy as to its administration, were handed down by the Commission in passing on specific questions raised in proceedings involving The North American Company (Holding Company Act Release Nos. 3405 and 3630), Engineers Public Service Company (Release No. 2897) and The United Gas Improvement Company (Release Nos. 2913 and 3511).

(6) A number of transactions proposed by registered holding companies or their subsidiaries pursuant to Section 11 (e) and other applicable sections, and

tending to effectuate partial or substantial compliance pith the requirements of Section 11 (b) (1), were approved by the Commission. The following holding companies were among those affected:

Associated Gas and Electric Corporation -- Holding Company Act Release No. 3353 (Section 11 (e) plan)

Columbia Gas & Electric Corporation -- Holding Company Act Release No. 3286

Community Power and Light Company -- Holding Company Act Release Nos. 3041, 3096

Engineers Public Service Company -- Holding Company Act Release No. 3230

Great Lakes Utilities Company -- Holding Company Act Release Nos. 3419, 3456

Lone Star Gas Corporation -- Holding Company Act Release Nos. 3589, 3591

Midland Utilities Company -- Holding Company Act Release Nos. 3250, 3145 (Section 11 (e) plan)

The North American Company -- Holding Company Act Release No. 2950

National Power and Light Company -- Holding Company Act Release No. 3612

The United Gas Improvement Company -- Holding Company Act Release No. 3433

The United Light and Power Company -- Holding Company Act Release Nos. 2991, 3189, 3242, 3316

Section 11 (b) (2) -- Corporate Simplification

This section of the Act makes it the duty of the Commission to require registered holding companies and their subsidiaries to take such steps “as the Commission shall find necessary to insure that the corporate structure or continued existence of any company in the holding company system does not unduly or unnecessarily complicate the structure, or unfairly or inequitably distribute voting power among security holders of such holding company system.” This section also provides that not more than three tiers of companies may be permitted in any holding company system and concludes with the proviso that “except for the purpose of fairly and equitably distributing voting power among the security holders of such company, nothing in this Paragraph shall authorize the Commission to require any change in the corporate structure or existence of any company which is not a

holding company, or of any company whose principal business is that of a public-utility company."

The important developments in the administration of Section 11 (b) (2) in the fiscal year may be summarized as follows:

(1) Under this provision the Commission instituted proceedings against the following companies:

The United Corporation -- Holding Company Act Release No. 2907

Florida Power & Light Company -- Holding Company Act Release No. 2874

International Utilities Corporation -- Holding Company Act Release No. 2885

Engineers Public Service Company -- Holding Company Act Release No. 2898

Pennsylvania Power & Light Company -- Holding Company Act Release No. 2906

Virginia Public Service Corporation -- Holding Company Act Release No. 2933

Illinois Iowa Power Company -- Holding Company Act Release No. 2953

Columbia Gas & Electric Corporation -- Holding Company Act Release No. 2963

New England Gas & Electric Association -- Holding Company Act Release No. 3035

New York Water Service Corporation -- Holding Company Act Release No. 3156

Pennsylvania Gas & Electric Corporation -- Holding Company Act Release No. 3251

Central Illinois Public Service Company -- Holding Company Act Release No. 3080

North American Light & Power Company -- Holding Company Act Release No. 3168

Consolidated Electric & Gas Company -- Holding Company Act Release No. 3225

Michigan Gas & Electric Company -- Holding Company Act Release No. 3408

Jacksonville Gas Company -- Holding Company Act Release No. 3434

Great Lakes Utilities Company -- Holding Company Act Release No. 3243

Cities Service Company -- Holding Company Act Release No. 3498

Republic Service Corporation -- Holding Company Act Release No. 3514

Southern Union Gas Company -- Holding Company Act Release No. 3586

Central Public Utility Corporation, Vt. -- Holding Company Act Release No. 3615

Northern States Power Company (Minn. & Del.) -- Holding Company Act Release No. 3595

(2) Section 11 (b) (2) hearings were held with respect to the following holding company systems:

Associated Gas and Electric Company -- File Nos. 591-30, 59-34

Central Public Utility Corporation -- File Nos. 59-40, 59-9

Cities Service Company -- File No. 59-46

Columbia Gas & Electric Corporation -- File No. 59-33

Community Gas and Power Company -- File No. 59-43

Electric Bond and Share Company -- File No. 59-26, 59-29

Engineers Public Service Company -- File No. 59-28

Federal Water Service Corporation -- File No. 59-35

Great Lakes Utilities Company -- File No. 59-45

International Utilities Corporation -- File No. 59-27

Middle West Corporation -- File Nos. 59-37, 59-41

The North American Company -- File Nos. 59-31, 59-39

Pennsylvania Gas and Electric Corporation -- File No. 59-36

Republic Service Corporation -- File No. 59-47

Southern Union Gas Company -- File No. 59-48

Standard Power and Light Corporation -- File Nos. 59-50, 59-51

The United Corporation -- File No. 59-25

(3) Orders were entered by the Commission prescribing action which companies in some of the major holding-company systems must take to comply with the simplification requirements of Section 11 (b) (2), including those in the following cases:

The Commonwealth & Southern Corporation -- Holding Company Act Release No. 3432

The Middle West Corporation -- Holding Company Act Release No. 3580

National Power & Light Company -- Holding Company Act Release No. 2962

North American Light & Power Company -- Holding Company Act Release No. 3233

Standard Power and Light Corporation -- Holding Company Act Release No. 3607

(4) A number of transactions proposed by registered holding companies or their subsidiaries pursuant to Section 11 (e) and other applicable sections, and tending to effectuate full or partial compliance with the requirements of Section 11 (b) (2), were approved by the Commission. The following companies were among those affected:

Associated Gas and Electric Corporation -- Holding Company Act Release No. 3137 (Section 11 (e) plan)

Columbia Gas & Electric Corporation -- Holding Company Act Release Nos. 3286, 3415

Derby Gas & Electric Corporation -- Holding Company Act Release No. 2875 (Section 11 (e) plan)

The Eastern Shore Public Service Company (Md.) -- Holding Company Act Release No. 3633

Federal Water Service Corporation -- Holding Company Act Release No. 3023

Great Lakes Utilities Company -- Holding Company Act Release No. 3419 (Section 11 (e) plan)

Jacksonville Gas Company -- Holding Company Act Release Nos. 3570 (Section 11 (e) plan)

Michigan Gas and Electric Company -- Holding Company Act Release No. 3599

The Middle West Corporation -- Holding Company Act Release No. 3580

National Power & Light Company -- Holding Company Act Release No. 3211 (Section 11 (e) plan)

Northern Indiana Public Service Company -- Holding Company Act Release Nos. 3145, 3250

North American tight & Power Company -- Holding Company Act Release No. 3658

North Shore Gas Company -- Holding Company Act Release Nos. 3131, 3199 (Section 11 (e) plan)

The United Light and Power Company -- Holding Company Act Release Nos. 2886, 2991, 3140, 3189, 3198, 3242, 3345

United Public Service Corporation -- Holding Company Act Release No. 3289

Virginia Public Service Company -- Holding Company Act Release No. 3562

Wisconsin Electric Power Company -- Holding Company Act Release No. 2950

Section 11 (e) provides a means whereby holding companies and their subsidiaries may file plans designed to bring about compliance with Section 11 (b). Twenty-nine such plans were filed during the fiscal year. Before a plan can be approved it must be found fair and equitable to persons affected thereby. An interesting example of the application of the Commission’s powers under Section 11 (e) and Section 11 (b) (2) respecting an operating company is the Jacksonville Gas Company case. Jacksonville Gas Company was on the verge of bankruptcy

but was able to file a voluntary reorganization plan pursuant to Section 11 (e) of the Act. In the space of a very short period of time, complete reorganization was approved and was duly enforced at the company's request in the United States District Court in Florida. [Footnote: For the Commission's opinion see Holding Company Act Release No. 3570. The Court's opinion approving the plan is reported, 46F. Supp. 852.]

Public Utility Financing

At the close of the last fiscal year, 65 applications and declarations pursuant to Sections 6 and 7 were pending, and 199 were filed during the year ended June 30, 1942. Of these, 164 were approved, 11 were withdrawn or dismissed, and 6 were denied, leaving 83 pending at the close of the fiscal year.

Of the 164 approved applications and declarations, 124 pertained to security issuance and 40 to assumption of liability and alteration of rights.

The issues covered by the 124 approved applications and declarations totaled $631,661,484. They were of the following types and for the following purposes:

Bonds: $383,172,000; 60.7%
Debentures: $14,000,000; 2.2%
Notes: $97,914,390; 15.5%
Preferred Stock: $70,377,900; 11.l%
Common Stock: $66,197,194; 10.5%
Total: $631,661,484; 100.0%

Refunding: $409,141,721; 64.8%
Reorganization: $1,500,000; 0.2%
Exchange for other securities: $56,977,273; 9.0%
Acquisition of property: $54,844,140; 8.7%
New financing: $90,742,750; 14.4%
Miscellaneous: $18,455,600; 2.9%
Total: $631,661,484; 100.0%

Competitive Bidding

The past year has provided the first opportunity for scrutiny of the operation of Rule U-50, which was adopted by the Commission on April 7, 1941 and became effective May 7, 1941. [Footnote: For a discussion of the reasons leading to the adoption of the rule, refer to the Seventh Annual Report.] This rule prescribes public invitation of sealed bids in connection with the sale of securities by registered public utility holding companies and their subsidiaries. From the

effective date of the rule to June 30, 1942, twenty-three security issues were sold at competitive bidding thereunder.

[table omitted]

Prior to the adoption of the competitive bidding rule, The Commission's staff had made a study of underwriting spreads prevailing during the five-year period ending January 1, 1940. It was found that slightly over one-half of the 19 utility mortgage bond issues covered by the study were sold by underwriters on the basis of a two-point spread and that the spread fell below that level in only four cases. The average spread for the 159 issues sold under the traditional method of private negotiation was 2.49 points ($2.49 per $100 bond).

As mentioned in Part I, under "Securities Effectively Registered", the cost of flotation of corporate securities was the lowest during this fiscal year that it has been in the approximately eight-year period over which the Commission has kept records thereof. The decline in underwriting spreads has been most noticeable in the offerings under Rule U-50. The spread in 6 of the 13 mortgage bond issues offered to the public following bids made under this rule was less than one point per issue, a circumstance not equaled in other recent corporate offerings except for a number of serial issues (principally railroad equipment issues which are also required to be sold through competitive bidding). [Footnote: The 18 bond issues for which bids were submitted under Rule U-50 included 15 mortgage issues of which 2 were bid in by insurance companies, 2 collateral trust issues, and 1 Debenture issue. All of the 16 offerings to the public were rated "bank quality" except the Debenture issue. All were offered within the fiscal year, except the 2 collateral trust issues which were offered just prior to the commencement thereof. One of the collateral trust issues (a serial note issue) was also offered with a spread of less than one point.] The spread, in percent of dollar proceeds registered for sale under the Securities Act, averaged 1.12 for the 15 "bank quality" bond issues offered to the public following bids made under this rule, compared with about 1.9 for 26 "bank quality" bond issues registered under the Securities Act and offered to the public between May 7, 1941 and June 30, 1942 but not subject to Rule U-50.

Exemption Cases

Generally speaking, Sections 2 and 3 of the Act contain definitions and exemption provisions pursuant to which the Commission determines whether companies are subject to the regulatory provisions of the Act.

In the past fiscal year the Commission disposed of applications filed by Moreau Manufacturing Company (Holding Company Act Release No. 2868), Pacific Gas and Electric Company (Holding Company Act Release No. 2988) and Public

Service Corporation of New Jersey (Holding Company Act Release Nos. 2998 and 3058), each of which sought to be declared not to be a subsidiary of specified companies. All of these applications were denied because the Commission could not find that the applicants were not subject to the controlling influence defined in Section 2 (a) (8) by the specified holding companies. Another case of importance was the application filed by Standard Oil Company (New Jersey) for exemption as a holding company pursuant to paragraph 3 of Section 3 (a). This application was also denied but the operation of the Commission's order was suspended for a period of six months because of the problems arising from the applicant's interest in other businesses and its expressed willingness to cooperate with the Commission in the solving of its problems under the Act (Holding Company Act Release Nos. 3312 and 3322).

During the year the Commission also granted or extended a number of exemptions under Sections 3 (a) (4), 3 (a) (5) and 3 (b) of the Act relating respectively to temporary holding companies, foreign holding companies and foreign subsidiaries. [Footnote: See Holding Company Act Release Nos. 3337, 3348, 3218, 3617, 3101, 3263, 2952, 2920, 3318, and 3263.]

Rules and Regulations

There were comparatively few changes in the Rules and Regulations under the Holding Company Act during the past fiscal year. [Footnote: Reference is made to the Seventh Annual Report of the Commission for a description of the general character of the rules adopted under the Holding Company Act, and the relationship of the Commission's rule-making powers to the administration of the Act.]

A change, in addition to that shown in the first footnote under Part II, in the rules to meet wartime conditions was an amendment to Rule U-7 (b), which defines an electric utility company for purposes of the Act. It exempts an industrial or other company which is not a subsidiary of a registered holding company, and which was not an electric utility company as of January 1, 1941, from being classified as an electric utility company by reason of any sales of surplus electric energy at wholesale during the existence of the national emergency, and for one year thereafter. [Footnote: Holding Company Act Release No, 3506, effective May 7, 1942.]

During the year a new provision was adopted to deal with the problem of equitable allocation of taxes between various companies in a holding company system which may join in filing a consolidated tax return. [Footnote: Rule U-45 (F) (6), Holding Company Act Release No, 2902, effective July 23, 1941. A later amendment was adopted to cover consolidated returns made under the Revenue Act of 1942, See Holding Company Act Release No, 4167.] There was also a

change, largely of an administrative character, in the Commission's Rules governing solicitation of security holders' authorizations regarding miscellaneous financial transactions. Under the amended rules, solicitations regarding a transaction which is itself the subject of Commission regulation are scrutinized in connection with the examination of other aspects of the proposed transaction. In cases where the solicitation is not part of a transaction subject to regulation (for example, solicitations in connection with an election of directors), the same rules are made applicable as have been adopted pursuant to the Securities Exchange Act for solicitation of proxies in respect of securities registration on a national securities exchange. [Footnote: Rules U-61 and U-62, effective July 15, 1941 and October 25, 1941, respectively. Holding Company Act Release Nos. 2836 and 3090.]

A number of minor changes were made by way of simplification and clarification of the forms under the Holding Company Act. [Footnote: See Holding Company Act Release Nos. 2899, 3249 and 3257. After the close of the past fiscal year a substantial reduction was made in the amount of information required in the Annual Supplement to the Registration Statement which registered holding companies must file under the Holding Company Act.]

PART IV

PARTICIPATION OF THE COMMISSION IN CORPORATE REORGANIZATIONS UNDER CHAPTER X OF THE BANKRUPTCY ACT, AS AMENDED

Summary of Activities

The Commission actively Participated in 148 reorganization proceedings involving the reorganization of 177 companies (148 principal debtor corporations and 29 subsidiary debtors). The aggregate stated assets of these 177 companies totaled approximately $2,044,933,000, and their aggregate indebtedness was approximately $1,317,556,000. For the first time the cases closed kept pace with the new cases in which the Commission filed a notice of appearance, there having been 34 of each during the year. The 114 proceedings, in which the Commission was actively participating as of June 30, 1942, involved 137 corporations (134 principal debtor corporations and 23 subsidiary debtors). These debtors had aggregate stated assets of approximately $l,753,306,000, and aggregate listed liabilities of approximately $$1,116,670,000.

With respect to the 34 new cases in which the Commission participated during the year, its notice of appearance was filed at the request of the judge in 12 proceedings, while in the remaining 22 the Commission entered its appearance upon the approval by the judge of the Commission's motion to participate. Of the 34 proceedings, 31 were instituted under Chapter X, and 3 under Section 77B. The debtors involved in these 34 proceedings had aggregate stated assets and aggregate indebtedness of approximately $128,389,000 and $92,423,000, respectively. [Footnote: Under Section 265a of the Bankruptcy Act, as amended, the Commission receives copies of every petition for reorganization filed under Chapter X and copies of other specified documents filed in the proceedings.]

The Commission As A Party To Proceedings

There have been no significant changes in the past fiscal year in the policies or practices of the Commission in performing its function under Chapter X, which have been described in previous annual reports. However, four years of experience by the Commission, the federal courts and the reorganization bar with the operation of Chapter X have reduced the amount of time required to be spent on purely procedural questions, and have permitted greater concentration of the Commission's energies upon substantive matters. There now exists a substantial number of precedents on nearly all important procedures and interpretive questions.

Plans of Reorganization Under Chapter X

The Commission's most important function under Chapter X is to aid the courts in effecting consummation of a fair and feasible plan of reorganization. After four years of experience there has been some change in the nature of the problems with which the Commission has to deal.

With respect to the fairness of plans, certain basic legal principles urged by the Commission throughout its activities under Chapter X are now firmly established as a result of the Supreme Court decisions in the Los Angeles Lumber and Consolidated Rock Products cases. [Footnote: 308 U.S. 106 and 312 U.S. 510, respectively.] The problem of fairness has become to a considerable extent one of studying and analyzing the law and facts of particular cases.

Perhaps the outstanding development in the Commission's Chapter X work during the fiscal year has been the increased importance and difficulty of problems of feasibility, including such questions as the adequacy of working capital, the relationship of fund debt or capital structure to property values, the adequacy of corporate earning power in relation to interest and dividend charges, the effect of proposed new capitalization upon the company's prospective credit, and the desirable objective that new securities shall not by their terms or

otherwise be deceptive to subsequent purchasers. Parties are inclined to gear their proposed capital structures to inflated war earnings, either because they do not recognize the extent to which the earnings are inflated or because they hope that the abnormal earnings will continue long enough to permit scaling down of debt to manageable proportions. The element of tax liability is an added force in the direction of excessive debt structures which promise interest deductions and sometimes other tax advantages which assume added importance in a period of high tax rates.

Although security holders' representatives frequently regard the fairness of the plan as their principal concern, the full protection of their interests requires also that the plan be feasible so that it win not hamper future operations or compel another reorganization. The extent to 'which the difficulties of debtors now in reorganization are attributable to previous non-feasible plans is apparent from an examination of the 34 cases in which a notice of appearance was filed by the Commission during the fiscal year. 17 involved companies which had already undergone reorganization since 1930, most of them under Section 77B since 1935. The Commission's insistence that plans should comply with reasonable standards of feasibility is designed to avoid a similar record as to Chapter X cases five or ten years hence and its continuing efforts in this respect constitute probably the most important phase of its present activities in connection with plans.

Advisory Reports on Plans of Reorganization

During the fiscal year the Commission prepared formal advisory reports with respect to plans of reorganization and supplemental reports with reference to amendments to such plans in the proceedings involving Sayre & Fisher Brick Company and Philadelphia and Reading Coal and Iron Company and also a third supplemental report in the proceedings involving Penn Timber Company in which an advisory report and two supplemental reports had previously been filed.

Appeals

Although the Commission may not appeal in a proceeding under Chapter X it participates in appeals taken by others. During the fiscal year the Commission took part in appeals in six proceedings.

In In re Ulen and Company the Commission urged attorneys for debenture holders were not entitled to compensation in a Chapter X proceedings for services rendered in a prior Chapter X proceedings which were not compensable under the rules prevailing in that type of proceeding. The District Court sustained this position and the Circuit Court of Appeals for the Second Circuit affirmed. In re Reynolds Investing Company involved the question whether a person who had

violated Section 249 of the Bankruptcy Act by purchasing or selling claims against or stock of the debtor while acting in a representative capacity was barred from allowance of compensation for services in a different representative capacity which had been assessed after the transactions in the debtor's securities had terminated. The Circuit Court of Appeals held, as urged by the Commission, that Section 249 barred allowance of compensation for any services performed by the applicant.

In Dana v. Securities and Exchange Commission the Circuit Court of Appeals for the Second Circuit sustained the position consistently taken by the Commission that a formal order of intervention is unnecessary to permit committees representing security holders to participate fully in proceedings under Chapter X. In re Marine Harbor Properties, Inc. involved the question of good faith in filing a petition by a debtor the property of which was subject to a certificated mortgage which had been reorganized in the New York State Courts pursuant to the provisions of the Shackno Act (New York Laws of 1933, C. 745) and the Mortgage Commission Act (New York Laws of 1935, C. 19). The Circuit Court of Appeals reversed the District Court's order approving the debtor's petition. Certiorari was granted by the Supreme Court, which upheld the Commission's contention that the debtor's participation in state court proceedings under the Shackno and Mortgage Commission Acts did not bar later resort to a proceeding under Chapter X, but affirmed the decision of the Circuit Court of Appeals upon the ground that the debtor had not sustained the burden of establishing its need for relief under Chapter X (Section 130) and the existence of good faith in filing the petition (Section 146). In re Paloma Estates, Inc. raised similar questions. Sims v. Fidelity Assurance Association involved the question whether the debtor was an insurance company eligible to file a petition under the Bankruptcy Act and questions as to whether the debtor's petition had been filed in good faith. The Commission urged approval of the debtor's petition and its position was sustained by the District Court. However, upon appeal the Circuit Court of Appeals reversed, holding that the debtor was an insurance company not eligible to seek relief under the provisions of the Bankruptcy Act and that the petition had not been filed in good faith because the interests of creditors would be best subserved in the receivership proceeding pending in West Virginia and other states. Certiorari was granted by the United States Supreme Court which, without deciding whether the debtor was an insurance company, concluded that the petition had been filed in good faith upon the ground stated by the Circuit Court of Appeals and upon the additional ground that it was unreasonable to expect that a plan of reorganization could be effected.

PART V

ADMINISTRATION OF THE TRUST INDENTURE ACT OF 1939

Information regarding the general purpose and scope of the requirements of the Trust Indenture Act of 1939, and the Commission's procedure in examining applications for qualification of indentures and trustee statements of eligibility and qualification for compliance with the statute, was set forth in the Sixth Annual Report of the Commission.

Since then a rule (Rule T-10B-3) has been adopted permitting a prospective trustee to obtain a declaratory ruling of the Commission as to whether or not it is an affiliate of a specified underwriter. This procedure is to enable complex questions of conflicting interests to be tried and decided in advance of any particular security issue, to avoid delaying securities transactions when they arise.

Under this rule J. P. Morgan & Co. Incorporated, a trust company, applied for a ruling at to its status in relation to Morgan Stanley & Co. Incorporated, an underwriting firm. The Commission held that the two houses were under common control within the meaning of the Act, and that J. P. Morgan & Co. Incorporated was therefore ineligible to act as trustee of Securities issued by any company for which Morgan Stanley & Co. Incorporated was an underwriter. [Footnote: Trust Indenture Act Release No. 15]

[statistical tables omitted]

PART VI

ADMINISTRATION OF THE INVESTMENT COMPANY ACT OF 1940

The past fiscal year marked the first full fiscal year in the administration of Investment Company Act of 1940. During the year the Commission concerned itself primarily with (1) the registration of companies subject to the Act; (2) the disposition of applications filed pursuant to the provisions of the Act seeking a determination of whether or not certain companies are investment companies within the meaning of the Act and applications requesting exemption from specific provisions of the Act; (3) the promulgation of rules prescribing the type of information and periodic reports to be filed with the Commission and the type of information and periodic reports required to be transmitted to security holders; and (4) the disposition of general administrative problems arising under the various sections of the Act.

Registration of Investment Companies

The first step in the regulation of investment companies provided by the Investment Company Act of 1940 is the requirement that all investment companies must register with the Commission. Registration is accomplished by filing a simple notification of registration with the Commission pursuant to Section 8 (a) of the Act. Most companies registered under the Act during the fiscal year ended June 30, 1941. However, 17 companies filed notifications of registration during the past fiscal year. Two of these 17 companies organized during the fiscal year and the others had not registered previously, either because they claimed an exemption from the provisions of the Act or for some other reason.

The next step in the registration process involves the filing with the Commission every registered investment company of a detailed registration statement pursuant to Section 8 (b) of the Act. These registration statements are filed in accordance with rules, regulations and forms promulgated by the Commission which are specifically designed for investment companies.

In addition to Form N-8B-1, which relates to management companies and was promulgated during the fiscal year ended June 30, 1941, the Commission has promulgated two new forms to be used for filing detailed registration statements. These forms are designated Form N-8B-2 and Form N-8B-3. Form N-8B-2 is designed for use by unit investment trusts which are currently issuing securities, and Form N-8B-3 is designed for use by incorporated management companies currently issuing periodic payment plan certificates.

The detailed registration statements contain complete information regarding each company, including certified financial statements, information regarding the organization of the company, management personnel and affiliated persons, compensation to officers, directors, and certain employees, capital structure, nature of assets, distribution and redemption of securities, information regarding the trustee and sponsor of the company and a recital of the policies of the company with respect to certain specified subjects.

In connection with the adoption of forms to be used for filing registration state under the Investment Company Act, the Commission also adopted rules which permit investment companies to file copies of information already filed under other Acts administered by the Commission in lieu of registration statements under the Investment Company Act, thereby gave effect to the directive of Congress as set forth in Section 8 (c) of the Act. These rules are designed to facilitate registration by companies which are subject to one or more of the other Acts administered by the Commission. Several companies have availed themselves of the privilege accorded by these rules.

Two hundred forty-five registered investment companies filed registration statements under the Act during the past fiscal year. Of these 245 registration

statements, 89 were filed by management open-end diversified companies, 8 by management open-end non-diversified companies, 62 by management closed-end diversified companies, 76 by management closed-end non-diversified companies, and 10 by unit investment trusts.

Every registration statement filed under the Act is carefully examined by the Commission's staff.

Periodic Reports to the Commission and to Security Holders

Section 30 (a) of the Investment Company Act provides that registered investment companies must file with the Commission such information, documents and reports as companies having securities registered on a national securities exchange are required to file with the Commission pursuant to Section 13 (a) of the Securities Exchange Act of 1943. Section 30 (b) of the Investment Company Act authorizes the Commission to require registered investment companies to file reports on a semi-annual or quarterly basis so as to keep reasonably current the information contained in the registration statements of such companies. The Commission promulgated two periodic report forms applicable to management investment companies during the past fiscal year. The periodic report forms for the other classes of investment companies had not been promulgated at the close of the fiscal year.

All registered management investment companies which filed detailed registration statements on form N-8B-1 are required to file annual reports on Form N-30A-1 within 120 days after the close of each fiscal year. The annual report form is designed to bring up to date as of the close of each fiscal year of the registrant, the information originally furnished by the registrant in its detailed registration statement. Form N-30A-1 is designed for use under both the Securities Exchange Act of 1934 and the Investment Company Act of 1940, and duplicate filings under these Acts are thereby eliminated.

All registered management investment companies which filed detailed registration statements on form N-8B-1 are required to file quarterly reports on Form N-30B-1 within 30 days after the close of each fiscal quarter. The quarterly report form requires only the minimum information necessary to be kept current to aid the Commission in the administration of the Act. This form is also designed for use under both the Securities Exchange Act of 1934 and the Investment Company Act of 1940, and supplants Form 8-K, the current report form under Securities Exchange Act of 1934, insofar as it is applicable to management investment companies having securities listed and registered on a national securities exchange.

One hundred ninety-six companies filed annual reports on Form N-30A-1 during the fiscal year ended June 30, 1942 and a like number filed quarterly reports on Form N-30B-1.

Section 30 (d) of the Act provides that every registered investment company shall transmit to its stockholders, and file with the Commission, at least semi-annually, reports containing certain prescribed information and financial statements. During the fiscal year ended June 30, 1942, 633 periodic reports to security holders were filed with the Commission.

Applications for Exemptions or Exceptions

Applications under Section 3 (b) (2) of the Act. A company which comes within the quantitative definition of an "investment company" as contained in Section 3 (a) (3) of the Act may apply to the Commission for an order pursuant to Section 3 (b) (2) of the Act, declaring it to be primarily engaged in a business other than that of an investment company. Such other business may be conducted either directly or through majority-owned subsidiaries or controlled companies conducting similar types of businesses. During the past fiscal year two such applications were denied, two other applications were denied under Section 3 (b) (2) although exemptions were granted under other sections of the Act, and four such applications were withdrawn. The Commission granted five applications pursuant to this section during the past fiscal year, and at June 30, 1942, fourteen applications were pending.

Other Applications for Exemptions. Section 6 (c) of the Act confers upon the Commission general exemptive powers if and to the extent that such exemption is necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policy and provisions of this title.

Eighty-one applications under this section were pending before the Commission during the last fiscal year. Of these 81 applications, 49 were filed during the last fiscal year and 70 were disposed of by the Commission during that period.

Section 6 (d) of the Act authorizes the Commission to exempt small closed-end investment companies from any and all provisions of the Act if the securities of such are not sold outside the states of incorporation and provided the exemption is not contrary to the public interest or inconsistent with the protection of investors.

Five applications under this section were pending before the Commission during the past fiscal year. Of these 5 applications, one was filed during the year and 4 were disposed of by the Commission during that period. With respect to the 4

applications which were disposed of, one was withdrawn and 3 were granted to a limited extent.

Dissolution of Investment Companies and Withdrawal of Registration Statements

Approximately 44 registered investment companies filed applications with the Commission during the fiscal year seeking orders of the Commission declaring that such companies had ceased to be investment companies within the meaning of the Act. These applications were filed pursuant to Section 8 (f) of the Act which provides that whenever the Commission on its own motion or upon application, finds that a registered investment company has ceased to be an investment company, it shall so declare by order, and upon the taking effect of such order the registration of such company shall cease to be in effect.

The Commission passed upon approximately 38 Section 8 (f) applications during the fiscal year. Of these 38 applications, 34 were granted, 2 were dismissed and 2 were denied. The applications that were granted involved companies which had formally dissolved and distributed all of their assets to their security holders, companies which had merged with other companies and transferred an of their assets to such other companies, and whose outstanding securities were owned by less than 100 persons and which were not making and did not presently propose to make a public offering of their securities. The last category of companies mentioned is excepted from the definition of “investment company” the provisions of Section 3 (c) (1) of the Act.

Affiliated Persons of Investment Companies

Transactions Between Investment Companies and Their Affiliated Persons. Section 17 the Act makes it unlawful for any affiliated person, promoter or principal underwriter for a registered investment company to sell to, or purchase securities or other property, or borrow money or other property from, the investment company or any company controlled by it. However, authority is given to the Commission to exempt, by order, any proposed transaction if evidence establishes that the terms of such transaction, including the consideration to be paid or received, are reasonable and fair and do not involve overreaching by any person concerned, and that it is consistent with the policies of the investment company recited in its registration statement and with the general purposes of the Act.

For the fiscal year ending June 30, 1942, there were 16 applications filed to exempt proposed transactions between affiliated persons and investment companies, or companies controlled by them. The Commission disposed of 5 of such applications after hearings; four were withdrawn without hearing, 1 was withdrawn after hearing and 6 are still pending. While the applications ostensibly

sought exemption of a proposed transaction involving the purchase and sale of securities, the disposition of such applications often included such matters as reorganizations and recapitalizations of investment companies, as well as affiliated non-investment companies.

PART VII
ADMINISTRATION OF THE INVESTMENT ADVISERS ACT OF 1940
Registration Statistics

As of June 30, 1941 there were registered with the Commission pursuant to the provisions of Investment Advisers Act of 1940 753 investment advisers, consisting of 420 sole proprietors, 123 partnerships and 210 corporations. On June 30, 1942 there were 732 investment advisers consisting of 411 sole proprietors, 123 partnerships and 198 corporations.

The following table sets forth information with respect to the status of the registration of investment advisers under the Act as of the end of the fiscal year:

As of 6/30/42

Applications filed/ 931
App. Pending/ 7
App. Withdrawn/ 6
Effective Registrations/ 732
Reg. Withdrawn/ 132
Reg. Cancelled/ 52
Denied/ 1
Revoked/ 1

In order to maintain reasonably current the information contained in the applications for registration, the Commission requires semi-annual reports to be filed by all registered investments advisers. These reports must be filed with the Commission within ten days after June 30, and December 31, of each year. Each registered investment adviser is required to disclose in the semi-annual report that after an examination of his original application for registration he finds either that (1) no changes have been effected in his business so that no amendments are required to the application for registration or (2) that changes have been effected in his business so that amendments are necessary for certain items in the original application for registration. If changes have been effected in business, amendments to the items affected are included in the semi-annual report.

Section 203 (d) of the Act empowers the Commission to deny, revoke or suspend the registration of an investment adviser if certain conditions exist. One of the

grounds for denying, revoking or suspending the registration of an investment adviser is the fact that such investment adviser within ten years prior to the registration has been convicted of a crime in connection with securities transactions or has been enjoined by a court from acting as an investment adviser, underwriter, broker or dealer.

In the exercise of its power under this section, the Commission has revoked the registration of one investment adviser. In this case it was found that the investment adviser in question had been enjoined by an order of the United States District Court from engaging in certain conduct and practices in connection with the purchase and sale of securities. In addition to this it was found that the application for registration contained material misstatements. It was also found that the investment adviser in question had converted to his own benefit certain moneys sent to him by clients for the purchase of securities, that he had purchased securities contrary to the authority of his clients and had converted the remaining balances to his own use.

Absence of Power to Inspect Books and Records of Investment Advisers

Section 209 (a) of the Act provides that whenever it appears to the Commission that the provisions of this Act have been or are about to be violated the Commission can institute a formal investigation for the purpose of determining whether there has been or is about to be a violation of the Act, The Act, however, does not confer upon the Commission the authority or duty to make periodic inspections of the accounts and records of registered investment advisers such as is conferred upon the Commission by Section 17 (a) of the Securities Exchange Act of 1934 with respect to registered broker-dealers. This omission leaves entirely unsupervised and unprotected a broad field in the handling of investment funds of the general public, Unfortunate situations involving large losses to clients have occurred which might have been averted if the Commission had authority to make regular periodic inspections of the accounts of registered investment advisers. The details of these situations and a further report to the Congress will be made concerning this matter.

PART VIII

OTHER ACTIVITIES OF THE COMMISSION UNDER THE VARIOUS STATUTES

LITIGATION

Civil Proceedings

At the beginning of the fiscal year ended June 30, 1942, 10 civil proceedings instituted by the Commission were pending; [Footnote: adjusted figure.] during the year, the Commission instituted 36 additional proceedings, including 33 injunctive actions brought against 91 persons to restrain them from fraudulent and otherwise illegal practices in the sale of securities. Of this total of 46 proceedings, 35 were disposed of during the fiscal year, including 2 cases which resulted in the entry of injunctions against 61 persons. 11 civil proceedings were pending at the end of the year.

Since its inception, the Commission has instituted a total of 440 civil proceedings and disposed of 429. Permanent injunctions have been obtained against 940 firms and individuals.

Data with respect to civil cases and appellate proceedings, including a brief description of all civil proceedings commenced or pending during the fiscal year and the status at the close of the year, are included among Appendix Tables 20 to 31. Some of the more important and interesting of these cases are described in more detail below.

Injunctive Actions Instituted by the Commission

Typical of the ingenious schemes to secure public investment in business enterprises without complying with the registration provisions of the Securities Act of 1933 was that involved in ***Securities and Exchange Commission*** v. ***Bailey.*** [Footnote: 41 F. Supp. 647 (S.D. Fla. 1941). Consent judgment entered January 26, 1942.] In this case the defendants were enjoined from selling investment contracts camouflaged as sales of land upon which tung trees were to be developed.

Another unorthodox form of securities was involved in ***Securities and Exchange Commission*** v. ***George Washington Memorial Park Cemetery Association***. [Footnote: D. N.J. Consent judgment against eight defendants entered April 8, 1942.] The defendants in this case had acquired unimproved rural land which they divided into cemetery lots and sold to purchasers in large quantities on an investment basis representing that cemetery lots constituted a sound investment. A large portion of the purchase price was to be used by the Association to make a number of contemplated improvements. To facilitate resale, the Association maintained a resale department through which purchasers might dispose of their lots. The Commission took the position that the factor of setting aside a portion of the purchase price for improvements designed to enhance the value of the land, coupled with the sale of multiple units and the resale provision, made the scheme merely a form of investment contract.

In ***Securities and Exchange Commission*** v. ***Hugh B. Monjar*** [Footnote: D. Mass. Pending at close of fiscal year.] the Commission charged the defendants with selling securities to members of the Mantle Club in excess of $1,340,000 in connection with transactions described by the defendants as “personal loans” to Hugh B. Monjar, organizer and head of the Club. The Commission contended that among the securities involved were “receipts” issued to the Club members and “subscription cards” and other instruments solicited from the members in connection with the “personal loans.”

In the case of ***Securities and Exchange Commission*** v. ***S. W. Funk*** [Footnote: S.D. Cal. Consent judgment entered Sept. 1941.] the Commission filed a complaint to enjoin the sale of profit-sharing agreements relating to oil and gas leases. The proceeds from the sale of these securities, which the defendants termed “mutual escrow agreements,” were used to finance the drilling of a test well within the area embraced by the leases.

In the first civil case involving Section 12 (h) of the Public Utility Holding Company Act, pertaining to political contributions, the Commission obtained a consent judgment enjoining Utah Power & Light Company from further violating that section [Footnote: D. Utah.]

Appellate Litigation under the Holding Company Act

Between May 15 and June 6, 1942, several of the largest holding company systems in the country filed petitions to review orders of the Commission requiring either geographical integration or corporate simplification or both under Sections 11 (b) (1) and 11 (b) (2) of the Public Utility Holding Company Act of 1935. [Footnote: ***Columbia Oil & Gas Co***. (C.C.S. 3d); ***United Gas Improvement Co***. (C.C.A. 3d); ***Commonwealth and Southern Corp.*** (C.C.A. 3d); ***North American Co.*** (C.C.A. 2d); ***Washington Railway and Electric Co.*** (App. D.C.).] These petitions represented the first major challenge of the constitutionality of the Holding Company Act since the original flood of litigation during the early days of that statute, which terminated when the Supreme Court sustained the constitutionality of the registration provisions in ***Electric Bond and Share Co.*** v. ***Securities and Exchange Commission*** 305 U. S. 419 (1938). After the close of the fiscal year the Second Circuit Court of Appeals affirmed the Commission’ s integration order against The North American Company [Footnote: ***North American Co***. v. ***Securities and Exchange Commission***, 133 F. (2d) 148 (C.C.A. 2d, Jan. 12, 1943.).] and the Third Circuit Court affirmed the simplification order against the Commonwealth and Southern Corporation. [Footnote: ***Commonwealth and Southern Corporation*** v. ***Securities and Exchange Commission***, F. (2d)_(C.C.A. 3d, March 31, 1943.).] Many other companies have not sought review but have complied with, or are in the process of complying with, Commission orders under the integration and simplification sections.

Another group of cases during the year involved petitions to review Commission orders denying application by public utility companies to be declared not subsidiaries of certain registered holding companies. Each of these orders was affirmed either during the fiscal year or after its close. [Footnote: ***Pacific Gas and Electric Co***. v. ***Securities and Exchange Commission***, 127 F. (2d) 378 (C.C.A. 9th, Apr. 14, 1942); rehearing granted and case still pending at close of fiscal year; ***Hartford Gas Co***. v. ***Securities and Exchange Commission***, 129 F. (2d) 794 (C.C.A. 2d, July 16, 1942); ***Public Service Corporation of New Jersey*** v. ***Securities and Exchange Commission***, 129 F. (2d) 899 (C.C.A. 3d, Aug. 12, 1942); ***American Gas and Electric Co***. v. ***Securities and Exchange Commission***, F***.*** (2d)_(App. D.C., Feb. 1, 1943.).] In addition, the Supreme Court on October 13, 1941, denied a petition for a writ of certiorari to review the previous year's judgment of the Sixth Circuit sustaining the Commission's order denying a similar petition by Detroit Edison Company [Footnote: ***Detroit Edison Co.*** v. ***Securities and Exchange Commission***, 199 F. (2d) 730 (C.C.A. 6th, May 12, 1941), ***cert denied***, 314 U.S. 618.]

In ***New York Trust Co.*** v. ***Securities and Exchange Commission,*** 131 F. (2d) 274 (C.C.A. 2d, Nov. 12, 1943), which was pending at the close of the fiscal year, the Court subsequently affirmed a Commission holding that the debenture holders of United Light and Power Company were entitled to the face value of their debentures and not to a redemption premium when the debentures were retired pursuant to an order of the Commission under the corporate simplification requirements of Section 11 (b) (2).

In ***Morgan Stanley and Co.*** v. ***Securities and Exchange Commission***, 126 F. (2d) 325 (C.C.A. 2d, Feb. 20, 1942), the Court affirmed the Commission's order in the ***Dayton Power and Light Company*** case. [Footnote: 8 S.E.C. 950, Holding Company Act Release No. 2693 (1941).] Rule U-12F-2, now superseded by the competitive bidding requirements of Rule U-50, prohibited the payment of any underwriter's fee on security issues if the underwriter stood in such a relation with the issuer that "there is liable to be or to have been an absence of arm's-length bargaining with respect to the transaction." The Commission's decision denied Morgan Stanley a $100,5000 underwriting fee which it would have received from Dayton Power & Light if there had been no violation of the rule.

In ***Chanery Corporation*** v. ***Securities and Exchange Commission***, 128 F. (2d) 303 (App. D.C., Apr. 27, 1942), the Court reversed an order of the Commission holding that preferred stock purchased by certain members of the management of Federal Water Service Corporation while they were engaged in formulating and presenting to the Commission plans of reorganization should not be allowed to participate in the reorganized corporation on a parity with other preferred stock. [Footnote: Holding Company Act Release No. 2635 (Sept. 24, 1941).] The

Commission had required those members to surrender that stock to the reorganized company at cost plus 4% interest. After the close of the fiscal year the Supreme Court of the United States affirmed the judgment of the Court of Appeals on the ground that the Commission's order had been erroneously based on "general equitable principles" apart from the statute. [Footnote: ***Securities and Exchange Commission*** v. ***Chenery Corporation***, 87 L. Ed. 411 (Feb. 1, 1943).] The Supreme Court directed that the case be remanded to the Commission for action not inconsistent with the Supreme Court's opinion.

Criminal Proceedings

The statutes administered by the Commission provide that evidence of violations may be transmitted to the Attorney General, who, in his discretion, may institute criminal proceedings. It is the Policy of the Commission to make a thorough investigation of alleged violations of the Acts and to consider carefully whether the evidence obtained merits criminal prosecution. If violations of the penal provisions are indicated, the results of such investigations and the supporting evidence are referred to the Department of Justice. Thereafter if criminal proceedings are instituted, the members of the Commission's staff who participated in the investigation assist the United States Attorneys in the preparation of the cases for presentation to the grand jury, in the trials which follow, and in the preparation of appellate briefs.

More evidence does not warrant prosecution under the Acts administered by the Commission, but violation of other statutes are indicated, the evidence is submitted to the appropriate state or federal agency. This results in the reference of quite a few cases to the postal authorities, to state commissions or other local enforcement authorities.

Up to July 1, 1942, the Commission had referred to the Department of Justice 378 cases, including 49 cases which were referred during the past fiscal year. Since organization of the Commission a total of 2,035 defendants have been indicted in 306 cases, including 27 cases which had been referred to the Post Office Department. During the past year indictments were returned against 183 defendants. Convictions have been obtained against 885 defendants in 216 cases, representing 91.3 percent of the 259 cases which have been disposed of as to principal defendants since the inception of the Commission. During the past fiscal year 142 defendants named in 44 cases were convicted.

Eight defendants have been convicted on indictments charging perjury arising out of Commission investigations. One defendant was acquitted.

The following table shows the comparative statistics with respect to criminal proceedings in cases developed by the Commission:

[table omitted]

Up to July 1, 1942, the Commission had caused to be instituted proceedings against 19 defendants for criminal contempt of court orders which had been obtained by the Commission. Of this number 13 were found guilty. One of these cases is now awaiting decision by the court.

A brief description of the criminal cases pending during the year ended June 30, 1942 showing their status on that date, is set forth in Appendix Tables 23, 24 and 27. A brief discussion of some of the more important cases follows

SECURITIES ACT OF 1933. -- Schemes to defraud uncovered in the enforcement of this Act are of infinite variety. Prosecutions during the year involved a large-scale cemetery promotion in Maine (***U. S.*** v. ***Paul F. Cassidy et al.)***; a pecan orchard in Southern Louisiana (***U. S.*** v. ***R. B. Brought et al***.); a popcorn vending machine company in Ohio (***U. S.*** v. ***F. E. Backmeier et al.***); an automotive patent venture in Los Angeles (***U. S.*** v. ***O***. ***F. Lundelius et al***.); an oil and gas lease promotion covering land in Texas and Oklahoma (***U. S.*** v. ***H. R. Edwards***); a mining company in Colorado (***U. S.*** v. ***Amos Downs et al.);*** and an industrial plant in Carrollton, Ohio (***U. S.*** v. ***Z. A. Gilbert et al.***) Even the religious beliefs and social proclivities of prospective investors have been utilized as a basis for promotional ventures which were made the subject of prosecution. For example, there is the Universal Order of Plenocrats in Chicago (***U. S.*** v. ***C. F. Davis et al.***); and the Mantle Club, centering in Wilmington and fanning out all over the country (***U. S.*** v. ***H. B. Monjar et al.)***

Many of these cases involved nation-wide solicitation of investments. In the ***Brough*** case, convictions were obtained in Oklahoma and five-year prison sentences imposed, more than $700,000 had been obtained by the defendants from about 1,400 investors residing in many different states. In the ***Monjar*** case, involving the Mantle Club, a socio-fraternal organization, investments had been obtained from people residing from Baltimore, Maryland to Portland, Oregon. In the ***Downs*** case, the stock of a mining company was sold in almost every state of the Union, as well as in the District of Columbia and in Canada. The defendants were tried and convicted in federal court at Denver.

The current prosecutions included a number involving efforts to evade the provisions of the securities laws by casting the enterprise into a form calculated to appear to be something other than an investment in securities as defined by the Act. For example, in the ***Brough*** case it was made to appear that the investors were purchasing pecan orchard acreage; in the ***Backmeier*** case that they were purchasing vending machines; in the ***Davis*** case that they were subscribing to memberships in a divinely inspired farm program; and in the

Monjar case that they were contributing to some transcendental program for the moral, as well as the financial, benefit of the members of the Mantle Club.

Also during the fiscal year a large number of convictions obtained in similar cases were affirmed by the appellate courts. These included the affirmance of convictions in Seattle for fraud in the sale of oil and gas leases (***J. F. Simons et al.*** v. ***U. S***.); convictions in Denver for fraud in the sale of stock of a cement company (***E. S. Gates*** v. ***U. S***.; ***C. S. Rice*** v. ***U. S***.); a conviction in Detroit for fraud in the sale of stock of a company making beer barrels (***J. K. Edlin*** v. ***U. S***.); convictions in California for the sale of oil leases, and interests therein, of properties in California (***A. Atherton et al***. v. ***U. S***.); a conviction for fraud in the sale of notes and trade acceptances issued by a whiskey rectifying company in Florida (***A. F. Fisher*** v. ***U. S***.); a conviction for fraudulent sale of securities of a mortgage company in Nebraska (***L. S. Holmes*** v. ***U. S***.); a conviction in New Mexico for the sale of stock in an insurance shares corporation (***S. C. Pandolfo*** v. ***U. S***.); and the conviction in New York of a certified public accountant for complicity in the fraudulent sale of stock of an industrial service company (***M. H. White*** v. ***U. S***.). In many of these cases only a few of the defendants appealed. In all of these cases the convictions were affirmed by the appellate courts.

SECURITIES ACT OF l934 -- Of the more outstanding of the prosecutions during the past year which arose from investigations under the 1934 Act, three involved stock market manipulations. In ***U. S.*** v. ***Ery Kehaya et al***. convictions were obtained in New York on charges of manipulating the New York Stock Exchange market for the common stock of Standard Tobacco Company in order to permit the defendants to unload large blocks of stock upon the unsuspecting public investors. It was charged that this was accomplished by means of the well known manipulative devices of wash sales, matched orders, and “touting” of the stock. Similar manipulative activity, this time on a regional stock exchange was involved in ***U. S***. v. ***Raymond R. Taylor***, where a prison sentence of approximately two years was imposed on Taylor for violations involving the market on the Detroit Stock Exchange, for stock of Mid-West Abrasive Company. In ***U. S.*** V. ***David Smart et al***., the manipulation involved a well known publishing concern, Esquire-Coronet, Inc. Convictions were obtained in Chicago against executives of the publishing concern and securities brokers of New York City, all of whom were charged with conspiring to raise artificially the price of the company’ s stock on the New York Curb Exchange in order to unloaded at the manipulated prices 200,000 shares of stock belonging to two of the defendants.

Another extremely important case which arose under the 1934 Act was that of ***U. S***. v. ***Russell W. McDermott***, a securities broker of Indianapolis, who was convicted of violations of the margin rules, fraud in over-the-counter transactions in securities with his own customers, and fraud perpetrated by means of excessive trading in a discretionary account. During the year the conviction of G.

A. Gantz, a securities broker of St. Louis on charges which involved operation of his business while insolvent and unauthorized use of customers' money, was affirmed by the Circuit Court of Appeals.

OTHER ACTS. Convictions were obtained during the year against Union Electric Company of Missouri on charges of making political contributions, made unlawful by Section 12 (f) of Public Utility Holding Company Act of 1935. Louis H, Egan, former president of the company, was found guilty of conspiracy to violate the same section, which makes it unlawful for a holding company or subsidiary thereof to make political contributions. The company was fined $80,000 and Egan was sentenced to two years' imprisonment, in addition to a fine of $10,000. Union Electric Company is a subsidiary of The North American Company. The indictment charged the defendants with setting up a "slush fund" accumulated through kick-backs from legal fees, payments to contractors and insurance agents, and the padding of expense accounts.

The conviction of Frank J. Boehm, former vice president of Union Electric Company, on charges of perjury was affirmed by the Circuit Court of Appeals, and the Supreme denied certiorari. The conviction was based upon perjury committed by Boehm while testifying before officers of the Commission in an investigation involving alleged violations of the anti-political contribution section of the 1935 Act.

The appeal of Howard G, Hopson, former president of the Associated Gas & Electric Company, was dismissed during the past year. He had been convicted of fraud in connection with the operation of the huge Associated Gas & Electric System.

An indictment was returned against one of the largest of the investment companies in an alleged fraud in the sale of 215,000 investment certificates in the face amount of $600,000,000 through an organization which extended into at least twenty-nine states. The indictment alleged that the defendants made use of deceptive financial statements, concealed artificial write-ups of securities values, manipulated trust funds, engaged in stock market manipulation, and operated while insolvent. The indictment was returned in Detroit. (***U. S***. v. ***Fidelity Investment Association et al***.)

An appeal during the year involved charges of defrauding an investment by a controlling person, Wallace Groves, whose conviction was affirmed by the Second Circuit Court of Appeals. The indictment had charged him with defrauding the General Investment Company in connection with sales to it of its own securities and payment of fictitious commissions on transactions pretended to be beneficial to the company. The conviction of George S. Groves was reversed. The Supreme Court denied certiorari to Wallace Groves.

COMPLAINTS AND INVESTIGATIONS

During the fiscal year ended June 30, 1942, the Commission received approximately 638 items of mail classified as “complaint-enforcement.” The major part of this mail consisted of letters from the general public seeking information, complaining of fraudulent or other illegal practices, and seeking various types of aid. The Commission has carefully considered and replied to every inquiry sent in by the public and investigated every complaint over which it has jurisdiction.

The complaint correspondence is a fruitful source of information for the Commission; it is mainly from this source that the Commission obtains important leads on securities violations. Other clues to irregularities in the investment field are obtained by the Commission from investigations made by its own staff or from other governmental voluntary agencies. The following chart gives some indication of the extent of the Commission’s investigatory activities:

[table omitted]

Through these investigations, and with the helpful assistance of such other agencies, the Commission has compiled a very extensive Securities Violations File which serves as a clearing house for information which is made available to those officials and agencies directly concerned with the eradication of illegal practices in the securities field. As of June 30, 1942, the Commission had assembled data concerning 41,065 persons and corporations against whom State or Federal action has been taken in connection with the sale of securities. During the past fiscal year approximately 5,170 items of information pertaining to existing files and 3,134 new names were added to those files.

INTERPRETATIVE AND ADVISOR SERVICE

The Commission has always recognized that the technical nature of the statutes it administers requires an interpretative and advisory service by the Commission to provide attorneys and the general public with prompt advice concerning problems arising under these statutes.

Inquiries are handled by correspondence as well as personal and telephone conferences.

The jurisdiction of the Commission does not extend to private disputes of a civil nature arising under the securities laws. Therefore, the Commission cannot advise litigants concerning the prosecution or defense in such cases. Where a civil suit between private parties has involved a disputed question of law under

the Acts administered by the Commission, however, the Commission has on occasion filed a brief with the court as ***amicus curiae*** in order to advise the court of its interpretation of the law as the agency administering it.

ACTIVITIES OF THE COMMISSION IN THE FIELD OF ACCOUNTING AND AUDITING

Effect of the War Effort

During the past year, accountants have been faced with many new and serious problems arising from the war effort and the earlier National Defense program. The Commission likewise, because of the importance which it attaches to financial statements has had to give careful consideration to these problems and to the need for all appropriate adjustments.

The Commission, in common with the accounting profession, has been especially interested in the maintenance of appropriate auditing standards. Fortunately, all concerned are agreed that the high standards of present practice should not be foregone. A principal difficulty has been the loss by most public accounting firms of much trained personnel to other phases of the war effort. Furthermore, a similar loss of accounting personnel by private business, coupled, in many instances, with a large new volume of war work, has meant that internal accounting and auditing controls, upon which the public accountant must rely in many respects, have in many instances suffered and hence, with a smaller or less experienced staff, the public accountant is often faced with the necessity of being even more painstaking in his audit.

Members of the Commission’s staff have cooperated with registrants and public accountants in exploring various means of meeting the situation. As a result, registrants have been encouraged to change their fiscal periods from a calendar year to a “natural business” year in an effort to lessen the year-end burden so as to utilize the public accountant’s services more efficiently. In Accounting Series Release No. 3115, the Commission outlined a special procedure and method of disclosure to be followed by registrants and their accountants where the press of war production prevented normal inventory-taking. It has also been indicated that lack of personnel could provide a proper basis for requesting an extension of time for filing annual reports with the Commission. Study of these problems is being continued and informal conferences are held as occasion warrants with individual accountants and with the appropriate committees of professional societies.

The Commission has also cooperated with various Federal war agencies through consultation and through utilization of its expert help for specialized work.

Cooperation with Professional Societies

The Commission has sought to cooperate with the accounting profession and to add to its full influence to that of the professional societies and others in a joint effort to maintain and raise accounting and auditing standards. As heretofore, the Commission, in its promulgation of rules or opinions on accounting matters, has, whenever applicable, invited the comments or suggestions of other Federal and State agencies interested in accounting, of committees of professional societies, and of other interested persons. Reciprocally, the Commission has been invited to offer suggestions or comments on proposed actions or bulletins of these organizations. The past year has produced much gratifying evidence as to the effectiveness of these activities.

Professional Conduct

While the Commission has cooperated with the accounting profession to secure an objective of high professional standards, yet it has, as it must, reserved to itself the right to invoke sanctions against accountants who willfully or carelessly violate its rules. During the past year the Commission for the first time found it necessary to invoke against an accountant the sanctions found in Rule II (e) of its Rules of Practice. In ***In the Matter of Abraham H. Puder, et al.,*** [Footnote: Securities Exchange Act of 1934, Release No. 3073 (1941).] the Commission, on the basis of stipulated facts, issued an order suspending Puder and the firm of Puder and Puder from practice before the Commission for three months. In ***In the Matter of Kenneth M. Logan,*** [Footnote: Accounting Series Release No. 28 (1942).] the accountant was denied the right to practice before the Commission for sixty days.

Accounting and Auditing

Several opinions involving accounting or auditing matters were issued by the Commission during the year. Of these, the case of outstanding significance was ***In the Matter of Associated Gas and Electric Company***, [Footnote: Securities Exchange Act of 1934, Release No. 3285A (1942).] a delisting proceeding under Section 19 (a) (2) of the Securities Exchange Act of 1934. The findings and opinion in the case contain an extensive criticism of various accounting practices followed in the financial statements of the registrant and of certain aspects of the certificates furnished by Haskins & Sells.

Other opinions under the Securities Act of 1933 and the Securities Exchange Act of 1934 dealt with the independence of the certifying accountant; [Footnote: ***In the Matter of Southeastern Industrial Loan Company***, Securities Act of 1933, Release No. 2726 (1941).] the adequacy of the representations made in an accountant's certificate; [Footnote: ***In the Matter of Automatic Telephone Dialer,***

Inc., Securities Act of 1933, Release No. 2736 (1941).] and the failure of financial statements to conform to sound accounting principals. [Footnote: ***In the Matter of Condor Gold Mining Company***, Securities Exchange Act of 1934, Release No. 3196 (1942); ***In the Matter of Comstock-Dexter Mines, Inc***., Securities Act of 1933, Release No. 2691 (1941).] In addition, many of the findings and opinions under other Acts administered by the Commission, particularly the Public Utility Holding Company Act of 1935, included discussion and decision of varied accounting issues.

Informal Consideration of Accounting Problems Raised in the Case of Individual Registrants

As in the past, the greatest part of the Commission's accounting and auditing activities stems from the examination of financial statements filed by particular registrants. Deficiency memoranda, issued against more than half of the financial statements currently filed, have continued to play an important role in securing satisfactory financial statements for investors. Also, accounting and auditing problems have been the subject of innumerable informal conferences between the Commission's staff and representatives of particular registrants. These conferences have proved to be an expeditious means of resolving difficult or unusual questions with respect to which no specific rules have been issued or the application of existing rules is uncertain.

SOLICITATION OF PROXIES, CONSENTS AND AUTHORIZATIONS

The Congress, three times, has in effect directed the Commission to adopt rules governing the solicitation of proxies. [Footnote: Section 14 (a) Securities Exchange Act of 1934; Section 12 (e) Public Utility Holding Company Act of 1935; Section 20 (a) Investment Company Act of 1940.] The Commission's proxy rules, which are contained in Regulation X-l4, require certain information to be made available to security holders whose proxies, consents or authorization are solicited.

During the fiscal year the Commission examined both the preliminary and final proxy material with respect to 1,655 solicitations and in each case commented on the material to the persons making the solicitation. In many cases it examined revised drafts of preliminary material. Aside from the initial material, 333 pieces of supplemental or "follow-up" soliciting material were received and examined. In addition to the regular examination which is made of all proxy material filed, the Commission continued its policy of furnishing every assistance to persons who desired to obtain informal opinions or suggestions in advance of the filing date.

REPORTS OF OFFICERS, DIRECTORS, PRINCIPAL SECURITY HOLDERS AND CERTAIN OTHER AFFILIATED PERSONS

The general purpose and scope of the ownership reporting requirements, prescribed by Section 16 (a) of the Securities Exchange Act of 1934, 17 (a) of the Public Utility Holding Company Act of 1935 and 30 (f) of the Investment Company Act of 1940 and the Commission's rules and regulations promulgated thereunder, as well as the procedures for obtaining the filing of required reports, examining them for compliance with the statutes and the rules, obtaining amended reports where necessary and the publication of information contained in the reports, have been described in the Sixth Annual Report of the Commission, pp. 180, 182 and previous annual reports.

[table omitted]

Form 4 is used for reporting changes in ownership of equity securities; Form 5 for reporting ownership of equity securities at the time an issuer for the first time secures registration of any equity security on a national security exchange; Form 6 for ownership of equity securities by additional persons who become officers, directors or principal stockholders; Form U-17-1 for reporting ownership of securities at the time a holding company becomes registered or an additional person becomes an officer or director; Form U-17-2 for reporting changes in ownership of utility securities; Form N-30F-1 for reporting ownership of securities at the time a closed-end investment company becomes registered or an additional person assumes any of specified relationships; and Form N-30F-2 for reporting changes in ownership of securities of closed-end investment companies.

PUBLICATIONS

Public Announcements

Under the various Acts it is the Commission's duty to publish its decisions and generally to inform Congress and the public of its activities. Its releases are classified into various categories so that a person may receive the material relating only to those phases of the Commission's work in which he is interested. The Commission has made an exhaustive check of its mailing lists to eliminate those no longer desiring specified material.

The announcements issued during the past fiscal year included 250 releases under the Securities Act of 1933; 320 under the Securities Exchange Act of 1934; 780 under the Public Utility Holding Company Act of 1935; 153 under the Investment Company Act of 1940; and 13 under the Investment Advisers Act of 1940. In addition, two releases concerned the Commission's activities in corporation reorganizations and six were issued under the Trust Indenture Act of 1939.

The following is a partial classification of the announcements by subject matter:

Opinions and orders/ 936
Reports on Court actions/ 111
Statistical data/ 138
Survey series/ 19

Other publications

Decisions and Reports of the Commission:

Buckram-Bound:
Volume 6 – October 1, 1939 to March 31, 1940
Volume 7 – April 1, 1940 to August 31, 1940
Volume 8 – September 1, 1940 to March 31, 1941

Report to Congress on the Study of Investment Trusts and Investment Companies:
Part Four, Chapter II:
Economic Significance of Investment Companies

Part Five:
Conclusions and Recommendations

(The decisions of the Commission and the reports to Congress on the Study of Investment Trusts and Investment Companies are for sale at the Government Printing Office, Washington, D. C., and a price list will be furnished upon request.)

Twenty-four semimonthly issues of the Official Summary of Stock Transactions and Holdings of Officers, Directors and Principal Stockholders

An Alphabetical List of Over-the-Counter Brokers and Dealers Registered with the Commission as of August 31, 1941

List of Securities Traded on Exchanges under the Securities Exchange Act of 1934, as of June 30, 1941, and as of December 31, 1941, together with the Supplements thereto

Report on Secondary Distributions of Exchange Stocks

(A complete list of the Commission's publications, the Rules of Practice or the Guide to Forms will be sent upon request made to the office of the Commission in Philadelphia, Pa.)

INSPECTION OF REGISTERED INFORMATION BY THE PUBLIC

Copies of any public information on file with the Commission, appearing in registration statements, applications, reports, declarations, and other public documents, are available for inspection in the Public Reference Room of the Commission at Philadelphia, Pa. During the past fiscal year more than 8,667 members of the public visited this Public Reference Room seeking such information, and thousands of letters and telephone calls were received requesting registered information. The Commission, through the facilities provided for the sale of public registered information, filled more than 2,127 orders for photocopies of material, involving 137,084 pages.

Insofar as practicable, the Commission has sought to make some of the public registered information filed with it available in its regional offices. In the New York Regional Office at 120 Broadway, facilities are provided for the inspection of certain public information on file with the Commission. This includes copies of (1) such applications for permanent registration of securities on all national securities exchanges, except the New York Stock Exchange and the New York Curb Exchange, as have received final examination in the Commission, together with copies of supplemental reports and amendments thereto, (2) annual reports filed pursuant to the provisions of Section 15 (d) of the Securities Exchange Act of 1934, as amended by issuers that have securities registered under the Securities Act of 1933, as amended. During the past fiscal year 10,241 members of the public visited the New York Office Public Reference Room, and more than 3,900 made telephone calls to this office, seeking registered public information, forms, releases, and other material.

In the Chicago Regional Office, which is located at 105 West Adams Street, there are available for public inspection copies of applications for permanent registration of securities on the Chicago exchanges, the New York Stock Exchange and the New York Curb Exchange, which have received final examination in the Commission, together with copies of all supplemental reports and amendments thereto. During the fiscal year ended June 30, 1941, more than 3,230 members of the public requested registered information, forms, releases, and other materials

In each of the Commission's regional offices there are available for inspection copies of prospectuses used in public offerings of securities effectively registered under the Securities Act of 1933, as amended. Duplicate copies of applications for registration of brokers or dealers transacting business on over-the-counter

markets, together with supplemental statements thereto, filed under the Securities Exchange Act of 1934, are also available for public inspection in the regional office having jurisdiction over the zone in which the principal office of the broker or dealer is located. Also, inasmuch as letters of notification under Regulation A exempting small issues of securities from the registration requirements of the Securities Act of 1933, as amended, may be filed with the regional office of the Commission for the region in which the issuer's principal place of business is located, copies of such material are available for inspection at the particular regional office where it is filed.

During the past fiscal year duplicate copies of applications for registration of Investment Advisers, together with supplemental statements thereto filed under the Investment Advisers Act of 1940, have been made available for public inspection in the regional offices having jurisdiction over the zone in which the principal office of the investment adviser is located.

There are available for inspection in the Commission's San Francisco and Cleveland Regional Offices, in which are provided complete facilities for such registration and qualification, copies of registration statements and applications for qualification of indentures filed at those regional offices.

Copies of all applications for permanent registration of securities on national securities exchanges are available for public inspection at the respective exchange upon which the securities are registered.

PUBLIC HEARINGS

The following statistics indicate the number of public hearings held by the Commission from July 1, 1935 to June 30, 1942:

[table omitted]

PERSONNEL

Commissioner Ganson Purcell was elected Chairman of the Commission on January 20,1942 for the term expiring June 30, 1942, vice Chairman Edward C. Eicher who resigned. On June 6, 1942 he was reappointed as Commissioner for the term expiring on June 5, 1947. Commissioner Purcell was reelected Chairman of the Commission on June 5, 1942 for the period ending June 30, 1943.

Edmund Burke, Jr., of New York, was appointed Commissioner July 31, 1941 for the term expiring June 5, 1944 vice Leon Henderson.

Robert H. O’Brien, of Montana, was appointed Commissioner on February 3, 1942 for the term expiring June 5, 1945 vice Edward C. Eicher.

The Commissioners, as of the close of the past fiscal year, were as follows:

Purcell, Ganson, Chairman
Healy, Robert E.
Pike, Sumner T.
Burke, Edmund, Jr.
O’Brien, Robert H.

As of the close of the past fiscal year the personnel of the Commission comprised five Commissioners and 1437 employees, of which 377 were assigned to the regional offices. These figures do not include 170 employees who had entered the military service and were carried on the payrolls in a furlough status. (As of May 21, 1943, the number of employees in the military service increased to 341.)

FISCAL AFFAIRS

[table omitted]