32nd Annual Report
of the
SECURITIES AND EXCHANGE COMMISSION

Fiscal Year Ended June 30, 1966

SECURITIES AND EXCHANGE COMMISSION
Headquarters Office
500 North Capitol Street
Washington, D.C. 20549

COMMISSIONERS

MANUEL F. COHEN, Chairman
BYRON D. WOODSIDE
HUGH F. OWENS
HAMER H. BUDGE
FRANCIS M. WHEAT

ORVAL L. DuBOIS, Secretary

LETTER OF TRANSMITTAL

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C.,
January 10, 1967

SIR : On behalf of the Securities and Exchange Commission, I have the honor to transmit to you the Thirty-Second Annual Report of the Commission covering the fiscal year July 1, 1965 to June 30, 1966, in accordance with the provisions of Section 23 (b) of the Securities Exchange Act of 1934, as amended; Section 23 of the Public Utility Holding Company Act of 1935; Section 46 (a) of the Investment Company Act of 1940; Section 216 of the Investment Advisers Act of 1940; Section 3 of the Act of June 29, 1949, amending the Bretton Woods Agreement Act; Section 11 (b) of the Inter-American Development Bank Act; and Section 11 (b) of the Asian Development Bank Act.
Respectfully,

MANUEL F. COHEN,
Chairman.

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

TABLE OF CONTENTS

Market value of securities available for trading

Share and dollar volume of stocks traded

Foreign stocks on exchanges

Comparative exchange statistics

Delisting of securities from exchanges

Unlisted trading privileges on exchanges

Applications for unlisted trading privileges

Block distributions reported by exchanges

Over-the-counter trading in common stocks traded on national securities exchanges

Manipulation and stabilization

Manipulation; market surveillance

Stabilization

Registration of over-the-counter securities

Periodic reports

Regulation of proxies

Scope of proxy regulation

Statistics relating to proxy and stockholder information statements

Stockholders' proposals

Ratio of soliciting to nonsoliciting companies

Proxy contests

Insiders' security holdings and transactions

Ownership reports

Recovery of short-swing trading profits by issuer

Investigations with respect to reporting provisions.

Regulation of broker-dealers and over-the-counter markets.

Registration

Administrative proceedings

Decisions of particular interest

Suspension of registration pending final determination

Net capital rule

Financial statements

Broker-dealer inspections

Supervision of activities of National Association of Securities Dealers, Inc

NASD disciplinary actions

Commission review of NASD disciplinary action

Commission review of NASD action on membership

Commission inspections of the NASD

Revision of rules, regulations and forms

Amendment of Rule 3a12-3

Amendments to the proxy rules

Amendment of Rule 15b6-1 and adoption of related Form BDW

Renumbering of rules under Sections 15 (b) and 15A and amendment of Rules 15A/2-1, 17a-5 and 19a3-1 to conform

Amendment of Rule 16a-2

Proposed amendment of Rule 16a-6

Financial position of corporations

Plant and equipment expenditures

Directory of registered companies

Stock market data

Opinions of the Commission

Procedures for publishing hearing examiners' initial decisions

Dissemination of information

Information available for public inspection

Publications

Organization

Personnel and financial management

COMMISSIONERS AND STAFF OFFICERS

Commissioners

MANUEL F. COHEN of Maryland, Chairman -- Term expires June 5, 1968

BYRON D. WOODSIDE of Virginia -- Term expires June 5, 1967

HUGH F. OWENS of Oklahoma -- Term expires June 5, 1970

HAMER H. BUDGE of Idaho -- Term expires June 5, 1969

FRANCIS M. WHEAT of California -- Term expires June 5, 1971

Secretary : ORVAL L. DuBois
Executive Assistant to the Chairman: DAVID L. RATNER

Staff Officers

EDMUND H. WORTHY, Director, Division of Corporation Finance.
ROBERT H. BAGLEY, Associate Director.

SOLOMON FREEDMAN, Director, Division of Corporate Regulation.
HAROLD V. LESE, Associate Director.
J. ARNOLD PINES, Associate Director.

LOUGHLIN F. McHUGH, Chief Economist, Office of Policy Research.

IRVING M. POLLACK, Director, Division of Trading and Markets.
THOMAS W. RAE, Associate Director.
EUGENE H. ROTBERG, Associate Director.

PHILIP A. LOOMIS, JR., General Counsel.
DAVID FERBER, Solicitor.
WALTER P. NORTH, Associate General Counsel.

ANDREW BARE, Chief Accountant.

LEONARD HELFENSTEIN, Director, Office of Opinions and Review.
W. VICTOR RODIN, Associate Director.
ALFRED LETZLER, Associate Director.

WILLIAM E. BECKER, Chief Management Analyst.

FRANK J. DONATY, Comptroller.

ERNEST L. DESSECKER, Records and Service Officer.

HARRY POLLACK, Director of Personnel.

REGIONAL AND BRANCH OFFICES

Regional Administrators

Region 1. New York, New Jersey -- Mahlon M. Frankhauser, 23rd Floor, 225 Broadway, New York, New York 10007

Region 2. Massachusetts, Connecticut, Rhode Island, Vermont, New Hampshire, Maine -- James E. Dowd, Suite 2203, John F. Kennedy Federal Building, Government Center, Boston, Mass. 02203.

Region 3. Tennessee, Virgin Islands, Puerto Rico, North Carolina, South Carolina, Georgia, Alabama, Mississippi, Florida, that part of Louisiana lying east of the Atchafalaya River -- William Green, Suite 138, 1371 Peachtree Street, N.E., Atlanta, Georgia 30309

Region 4. Illinois, Indiana, Iowa, Kansas City (Kansas), Kentucky, Michigan, Minnesota, Missouri, Ohio, Wisconsin -- Thomas B. Hart, Room 1708, U.S. Courthouse and Federal Office Building, 219 South Dearborn Street, Chicago, Illinois 60604

.Region 5. Oklahoma, Arkansas, Texas, that part of Louisiana lying west of the Atchafalaya River, and Kansas (except Kansas City) -- O. H. Allred, 503 U.S. Court House, 10th & Lamar Streets, Fort Worth, Texas 76102

Region 6. Wyoming, Colorado, New Mexico, Nebraska, North Dakota, South Dakota, Utah -- Donald J. Stocking, 7224 Federal Building, 1961 Stout Street, Denver, Colorado 80202

Region 7. California, Nevada, Arizona, Hawaii, Guam -- Arthur E. Pennekamp, 450 Golden Gate Avenue, Box 36042, San Francisco, California 94102

Region 8. Washington, Oregon, Idaho, Montana, Alaska -- James E. Newton, 900 Hoge Building, Seattle, Washington 98104

Region 9. Pennsylvania, Maryland, Virginia, West Virginia, Delaware, District of Columbia -- Alexander J. Brown, Jr., 500 North Capitol Street, Washington, D.C. 20549

Branch Offices

Cleveland, Ohio, 44113 -- Room 1628, Standard Building, 1370 Ontario Street.

Detroit, Michigan, 48226 -- Room 1503, Washington Boulevard Building, 234 State Street.

Houston, Texas, 77002 -- Room 2606, Federal Office Annex, Courts Building, 515 Rusk Ave.

Los Angeles, California, 90028 -- Room 309, Allstate Title Building, 6331 Hollywood Blvd.

Miami, Florida, 33130 -- Room 1504, Federal Office Building, 51 S. W. First Ave.

St. Louis, Missouri, 63102 -- Room 916, Federal Building, 208 North Broadway.

St. Paul, Minn., 55101 -- 1027 Post Office Building, 180 East Kellogg Blvd.

Salt Lake City, Utah, 84111 -- Room 6004, Federal Building, 125 South State Street.

COMMISSIONERS

Manuel F. Cohen, Chairman

Chairman Cohen was born in Brooklyn, N.Y., on October 9, 1912. He holds a B.S. degree in social science from Brooklyn College of the College of the City of New York. He received an LL.B. degree, cum laude, from Brooklyn Law School of St. Lawrence University in 1936, and was elected to the Philonomic Council. He is a member of the District of Columbia and New York bars. In 1933-1934 he served as research associate in the Twentieth Century Fund studies of the securities markets. Chairman Cohen joined the Commission's staff as an attorney in 1942 after several years in private practice, serving first in the Investment Company Division and later in the Division of Corporation Finance, of which he was made Chief Counsel in 1953. He was named Adviser to the Commission in 1959 and in 1960 became Director of the Division of Corporation Finance. He was awarded a Rockefeller Public Service Award by the trustees of Princeton University in 1956 and for a period of 1 year studied the capital markets and the processes of capital formation and of government and other controls in the principal financial centers of Western Europe. In 1961, he was appointed a member of the Council of the Administrative Conference of the United States and received a Career Service Award of the National Civil Service League. From 1958 to 1962 he was lecturer in Securities Law and Regulation at the Law School of George Washington University and he is the author of a number of articles on securities regulation published in domestic and foreign professional journals. In 1962, he received an honorary LL.D. degree from Brooklyn Law School. He took office as a member of the Commission on October 11, 1961, for the term expiring June 5, 1963, and was reappointed for the term expiring June 5, 1968. He was designated Chairman of the Commission on August 20, 1964.

Byron D. Woodside

Commissioner Woodside was born in Oxford, Pa., in 1908, and is a resident of Haymarket, Va. He holds degrees of B.S. in economics from the University of Pennsylvania, A.M. from George Washington University, and LL.B. from Temple University. He is a member of the bar of the District of Columbia. In 1929 he joined the staff of the Federal Trade Commission, and in 1933, following the enactment of the Securities Act of 1933, was assigned to the Securities Division of that Commission which was charged with the administration of the Securities Act. Commissioner Woodside transferred to the Securities and Exchange Commission upon its establishment by the Securities Exchange Act of 1934. In 1940 he became Assistant Director and in 1952 Director of the Division (now Division of Corporation Finance) responsible for

administering the registration and reporting provisions of the Securities Act, Securities Exchange Act, the Trust Indenture Act of 1939, and, in part, the Investment Company Act of 1940. For 14 months commencing in May 1948, he was on loan to the Department of the Army and assigned to duty in Japan as a member of a five-man board which reviewed reorganization plans of Japanese companies under the Occupation's decartelization program; and beginning in December 1950, he served 17 months with the National Security Resources Board and later with the Defense Production Administration as Assistant Deputy Administrator for Resources Expansion. He took office as a member of the Securities and Exchange Commission on July 15, 1960, for the term of office expiring June 5, 1962, and was reappointed effective June 5, 1962, for the term expiring June 5, 1967.

Hugh F. Owens

Commissioner Owens was born in Muskogee, Oklahoma on October 15, 1909, and moved to Oklahoma City in 1918. He graduated from Georgetown Preparatory School, Washington, D.C., in 1927, and received his A.B. degree from the University of Illinois in 1931. In 1934, he received his LL.B. degree from the University of Oklahoma College of Law, and became associated with a Chicago law firm specializing in securities law. He returned to Oklahoma City in January 1936, to become associated with the firm of Rainey, Flynn, Green and Anderson. From 1940 to 1941, he was vice-president of the United States Junior Chamber of Commerce. During World War II he attained the rank of Lieutenant Commander U.S.N.R. and served as Executive Officer of a Pacific Fleet destroyer. In 1948, he became a partner in the firm of Hervey, May and Owens. From 1951 to 1953, he served as counsel for the Superior Oil Company in Midland, Texas, and thereafter returned to Oklahoma City, where he engaged in the general practice of law under his own name. He also served as a part-time faculty member of the School of Law of Oklahoma City University. In October 1959, he was appointed Administrator of the then newly enacted Oklahoma Securities Act and was active in the work of the North American Securities Administrators, serving as vice-president and a member of the executive committee of that Association. He took office as a member of the Securities and Exchange Commission on March 23, 1964, for the term expiring June 5, 1965, and was reappointed for the term expiring June 5, 1970.

Hamer H. Budge

Commissioner Budge was born in Pocatello, Idaho, on November 21, 1910. He attended the College of Idaho, Caldwell, Idaho, received an A.B. degree from Stanford University, Palo Alto, California, majoring in political science, and an LL.B. degree from the University of Idaho in Moscow, Idaho. He is admitted to practice before the Supreme Court of Idaho and the Supreme Court of the United States and practiced law in the city of Boise, Idaho, from 1936 to 1951, except for 3 1/2 years in the United States Navy (1942-1945), with final discharge as Lieutenant Commander. Elected to the Idaho State Legislature, he served three sessions, two as assistant Republican floor leader and one as

majority floor leader. First elected to Congress in November 1950, he represented Idaho's Second Congressional District in the United States House of Representatives during the 82d, 83d, 84th, 85th, and 86th Congresses. In the House he was a member of the Rules Committee, Appropriations Committee, and Interior Committee. During the period from 1961 until his appointment to the Commission he was District Judge in Boise. He took office as a member of the Securities and Exchange Commission on July 8, 1964, for the term of office expiring June 5, 1969.

Francis M. Wheat

Commissioner Wheat was born in Los Angeles, California, on February 4, 1921. He received an A.B. degree in 1942 from Pomona College, in Claremont, California, and an LL.B. degree in 1948 from the Harvard Law School. At the time of his appointment to the Commission, Commissioner Wheat was a member of the Los Angeles law firm of Gibson, Dunn & Crutcher, with which he became associated upon his graduation from law school. His practice was primarily in the field of corporation and business law, including the registration of securities for public offering under the Securities Act of 1933. He has been active in bar association work, including service as Chairman of the Committee on Corporations of the Los Angeles County Bar Association and Chairman of the Subcommittee on Investment Companies and Investment Advisers, Committee on Federal Regulation of Securities, American Bar Association (Banking and Business Law Section). He also has written or co-authored articles on various aspects of the securities business and its regulation, both under Federal and State law. He took office as a member of the Commission on October 2, 1964, for the term expiring June 5, 1966, and was reappointed for the term expiring June 5, 1971.

INTRODUCTION

Changing Conditions in the Securities Industry-Changes are taking place in the nation's securities markets and the securities industry. The dramatic growth of institutional investment in equity securities and the advent of automation are but two examples of the changes which raise basic questions about the structure of the securities industry and its ways of doing business. The Commission must continually study and assess the implications of these changes and take appropriate action if it is to fulfill its statutory obligations and help to maintain public confidence in the securities markets.

The Commission has recently completed and submitted to the Congress a Report on the Public Policy Implications of Investment Company Growth. The Report was submitted pursuant to Section 14 (b) of the Investment Company Act of 1940, which authorizes the Commission, "if it deems that any substantial further increase in the size of investment companies creates any problem involving the protection of investors or the public interest, to make a study and investigation" and "to report the results of its studies and investigations and its recommendations to the Congress."

Both the securities industry and the Commission have taken important first steps in the use of electronic data-processing equipment, but much remains to be done in that area. The Commission's computer is already serving an important role in the surveillance of the securities markets and in developing a better understanding of the operation of the securities markets. The Commission is also working with the self-regulatory organizations, namely, the national securities exchanges and the National Association of Securities Dealers, to develop automated procedures which will make possible more efficient and effective procedures for the execution of securities transactions, the publication of more timely and informative price and other information, and the establishment of improved surveillance programs.

The Commission staff has drafted improved financial reporting forms for broker-dealers and investment advisers, and is discussing these forms with industry groups. The information derived from these forms, coupled with the use of computer simulation techniques, should facilitate the evaluation of trends and problems within the industry and of the effects of alternative regulatory actions.

Changes in the securities markets and in the companies whose securities are traded require a reassessment of the Commission's disclosure requirements. At the present time the Commission is working with the accounting profession and corporate executives to improve financial reporting by "conglomerate" companies and to enhance the comparability of financial statements of similar companies. In addition the Commission is reviewing its disclosure requirements under the Securities Act of 1933 and the Securities Exchange Act of 1934 to determine if the requirements can be coordinated and simplified so as to provide more meaningful information to investors.

In sum, changes in the structure of the securities markets, in the composition of the investor population, and in technology all require knowledge and understanding on the Commission's part and imaginative regulation to deal with the problems raised. The Commission's budget and staff have been strained in an effort to keep pace with these problems. The Commission is attempting, through improved coordination and cooperation with the states and the self-regulatory bodies and other measures, to achieve the best utilization of its available resources.

PART I
IMPORTANT RECENT DEVELOPMENTS

As indicated in the Introduction to this Report, the Commission and its staff devoted considerable attention during the 1966 fiscal year to the study of changes taking place in the securities field and consideration of the appropriate regulatory response. Some of the problem areas had been touched on in the Report of the Special Study of Securities

Markets and various of the actions taken during the year were to implement recommendations of that Study. Another important step forward was the acquisition of a computer, coincident with the Commission's move into a new building. The computer will contribute substantially to the Commission's efforts to discharge its responsibilities more effectively. The sections that, follow describe in brief the principal matters under consideration during the year (aside from developments with respect to the Securities Acts Amendments of 1964 which are discussed in Part II of this Report), the long-awaited move to satisfactory quarters, and the Commission's entry into the computer age.

Proposed Broker-Dealer Financial Reports

The Commission has submitted to industry leaders an informal proposal to require broker-dealers to furnish increased financial information on a periodic basis.

In making this proposal, the Commission considered several factors. It noted that this is a period of rapid change in the securities markets and the security industry. The resulting situation calls for actions and decisions which require an informed analysis of the operations of the markets and of persons and organizations in the markets. It is necessary to evaluate the effects which various changes and proposals by the Commission and others may have on the functioning of the industry, its profitability and its ability to attract capital and people with the imagination and energy so necessary to the continued growth and development of our national economy. The Commission believes that a full regulatory response to these conditions should be based on informed analysis of the economic factors at work in the industry. The Commission, the stock exchanges and the National Association of Securities Dealers, Inc. now receive assorted financial information at various times but often in a form which does not permit meaningful evaluation and there is an almost complete absence of information about the sources of income and expense for large segments of the industry. Conferences with industry leaders are continuing.

Level and Structure of Commission Rate

During the fiscal year, the staff continued its research on the level of the exchange commission rate. Considerable effort was devoted to improving the quality and quantity of available data. As noted above a proposed report form for broker-dealers has been drafted. Pending resolution of the problems in developing such a report, the New York Stock Exchange, following conferences with the Commission staff, improved and made mandatory the filing of the Exchange's income and expense report by all members doing a public commission business. It also adopted a form to provide supplementary balance sheet information for the firms filing such reports.

The Commission staff has also continued its consultations on the commission rate structure with the New York Stock Exchange staff and others. These were directed towards gaining a fuller understanding of the various practices which now permit

arrangements qualifying the fixed minimum commission schedule established by the Exchange. Based partly on these discussions, the Commission, with a view to insuring a reasonable commission rate structure, has been evaluating such current practices as "give-ups" and "give-aways", reciprocal arrangements, and the provision of special services.

Odd-Lot Studies

The Special Study recommended that the New York Stock Exchange, with appropriate participation by the Commission, undertake a cost study of the odd-lot business. It also recommended that the Commission, in conjunction with other exchanges, undertake studies of the methods and costs of handling odd-lots on those exchanges. During the fiscal year the Commission reviewed the odd-lot differential charged by New York Stock Exchange firms in the light of the cost studies of the Exchange discussed in last year's annual report, the analysis made by the Commission's staff, and the numerous conferences with the exchanges on the matter.

On June 16, 1966, effective July 1, 1966, the New York Stock Exchange, at the request of the Commission, adjusted its odd-lot differential. The new differential is 12^ cents on each share of stock selling for less than $55 and 25 cents on each share selling for $55 or over. The previous "break point" was $40. In requesting this change the Commission indicated that it expected that a further review of the odd-lot differential charge of the New York Stock Exchange would be made promptly after the end of 1966. In addition, the Commission determined to extend its inquiry into the mechanics and principles under which odd-lot transactions are effected in all securities markets. It has requested the comments of all the exchanges and the NASD with regard to a number of significant issues and problems pertinent to such a study.

Review of Exchange Rules Regarding Off-Board Trading

The Special Study Report recommended that the Commission and its staff give continuing attention to "factors contributing to or detracting from the public's ready access to all markets," as well as limitations on competition between markets and the effects of such limitations on the fair and orderly functioning of the markets.

Until recently Rule 394 of the New York Stock Exchange prohibited all off-board transactions in listed securities, whether effected on a principal or agency basis, unless the securities are specifically exempted by the Exchange. The other national securities exchanges have similar rules. Near the close of fiscal 1965 the Commission's staff began a study to determine whether such prohibitions were consistent with the standards established under Section 19 (b) of the Securities Exchange Act for fair dealing in securities traded on exchanges. This inquiry was conducted during fiscal 1966. Following the end of the year, the Exchange, at the request of the Commission, amended Rule 394 to permit member broker-dealers to execute transactions with certain non-member

broker-dealers who maintain markets in listed securities. The rule is designed to promote competition between the exchange specialist and the non-member market-maker and to provide the public customer with the benefits of the best available market.

Automation of Market Facilities

During the past year the Commission appointed certain members of its staff to an Electronic Data Processing Committee. The Committee's responsibilities include (1) the continuous examination of industry practices and Commission rules to insure that the development and use of automation in the securities industry fulfills the needs of both the industry and the Commission; and (2) the recommendation of policies and procedures to implement its findings.

The Committee has met with representatives of the various exchanges, the National Association of Securities Dealers, suppliers of stock market data and other interested parties to discuss various aspects of automation in the securities industry. Discussions with the exchanges have dealt with such matters as the establishment of central bookkeeping systems and central depositories for securities, the improvement of quotations, the automation of surveillance procedures and the clearing operation, and the automation of the execution of odd-lot transactions. Automation in the over-the-counter market has been discussed with the National Association of Securities Dealers, with broker-dealers, and with vendors who hope to supply the equipment and related services for any such program.

In recent years the New York Stock Exchange has worked toward the development of a centralized system for the handling and delivery of securities through the use of automated procedures. To further the development of such systems, the Commission during fiscal year 1966 amended Rules 8c-1 and 15c2-1 under the Exchange Act to provide that the hypothecation of customers' securities held by a clearing corporation or other subsidiary organization of a national securities exchange or national securities association or by a custodian bank pursuant to a central system in which customers' securities are commingled with securities of others will not of itself constitute a commingling prohibited by those rules. Generally speaking, the exemption is available only where the custodian agrees to deliver the securities it holds as directed by the system and not to assert any claim against them; the system has safeguards for the handling, transfer and delivery of the securities; and the system provides for fidelity bond coverage of employees and agents of the clearing corporation or other subsidiary organization and for periodic examination by independent public accountants. In addition, the Commission must find that the custody agreement and the safeguards established are adequate for the protection of investors. At the time the Commission amended the rules it found that the New York Stock Exchange's Central Certificate Service met the specified standards.

While the amendment makes clear that the presence within a system of a stock certificate representing the interests of various customers and other parties, including pledgees, does

not constitute a prohibited commingling, it does not make legal a hypothecation prohibited by Rules 8c-1 and 15c2-1. Thus, it would still constitute a violation of these rules to hypothecate the securities of more than one customer of a member, broker or dealer to secure a loan unless the consent of each customer is obtained, or to hypothecate the securities of a customer with those of any person other than a customer to secure a loan.

Over-the-Counter Markets

The Special Study pointed out serious inadequacies in the supervisory controls utilized by broker-dealers in their surveillance of the selling activities of salesmen and other employees and recommended the strengthening of such procedures and the adoption by the self-regulatory agencies of clearer standards and stronger enforcement procedures to assure more effective supervision by their member firms.

The Commission's staff initiated discussion with the NASD to deal with these problems and on July 1, 1965, the NASD adopted rules dealing with supervision procedures and selling practices of Association members. Among other things, these rules require the establishment and enforcement of written supervisory procedures and designation of a partner or officer to be responsible for their execution. The internal procedures must include periodic review of customer accounts and at least an annual inspection of each branch office. The NASD rule governing discretionary accounts has also been amended to require written customer authorization, supervisory review, and approval of activity in such accounts. A revised statement summarizing many of the selling practices which violate a member's responsibility for fair dealing also was adopted. To aid in the implementation of these new rules, the Association has prepared and distributed to its members a separate comprehensive manual which contains detailed guidelines and suggestions for effective supervisory procedures. All of these areas were subjects of Special Study recommendations.

During the year a number of further conferences were held between the NASD and the Commission staff concerning the NASD markup policy. The NASD has had a special committee reviewing the Association's markup policy, which also was the subject of a number of significant recommendations by the Special Study. The Association hopes to present a revised markup policy to its Board of Governors for adoption in the near future.

As noted in last year's annual report, the NASD engaged an outside management consulting firm to study the effects of its revised newspaper quotations system which was adopted in response to the provisions of Section 15A (b) (12) of the Securities Exchange Act as amended in 1964 and the recommendations of the Special 'Study. The study was also designed to assist in evaluating the possible effects and appropriateness of the Special Study's recommendations regarding the prohibition of so-called "riskless" principal transactions in the over-the-counter markets and the disclosure of prevailing inter-dealer markets to investors. In October 1966, the findings and conclusions of the

study were announced by the NASD. The study found that the quotations revisions made in 1965 had had no substantial impact on the markets for the securities affected, and that the issuers of these securities as well as well as those quoted in local lists sponsored by the NASD favored publication of inter-dealer (i.e. wholesale) quotations. The NASD has revised its rules to provide that all over-the-counter quotations in national news media reflect inter-dealer markets including those in securities traded only on a local basis. With respect to the possible impact of adoption of the other Special Study proposals, the consulting firm concluded that certain types of NASD members would be adversely affected. These conclusions are now being reviewed by the Commission's staff.

Coordination of Regulatory Efforts

During the past year, the Commission gave increased emphasis to the coordination of its regulatory activities with those of the various states and the self-regulatory institutions to improve the effectiveness of regulation and at the same time to reduce the burdens of compliance. The regional offices took steps to improve the coordination of inspection and other activities with state securities administrators and with the NASD in those areas where the respective jurisdictions overlap. Staff members of the Commission and of certain of the state authorities have conducted joint inspections which have strengthened and made more effective the entire inspection program.

The Commission has also developed procedures for informing state administrators about important investigations the Commission is conducting in their respective states and for advising them of injunctive or public administrative proceedings which are to be instituted there.

To make information filed with the Commission more readily available to the states, the Commission now furnishes to the interested state administrators a copy of the prospectus in the first registration statement filed by a company under the Securities Act of 1933. The Commission will also send a copy of any broker-dealer withdrawal form to the state administrator in the state in which the firm's principal office is located. This form may help the state administrator determine whether any regulatory action under state law is appropriate.

To reduce the burden on persons filing broker-dealer application forms, the North American Securities Administrators recently approved the adoption of a uniform form, which will be available to all administrators. A common core of information would be provided by the Commission's broker-dealer registration form, and that information would be supplemented by information, if any, required by a particular jurisdiction. This new form will reduce the burden on firms who must now furnish the same or similar information to various regulatory bodies.

Significant progress has also been made to coordinate the administration of examinations given to securities salesmen, to relieve them of the need to take essentially duplicative

examinations. In its examination program for persons associated with broker-dealers that are not members of the NASD, the Commission grants reciprocity to securities examinations meeting established standards. Since the initiation of the Commission examination program in January 1966, a majority of the 31 states which require salesmen to pass a general securities examination, and the NASD, have granted reciprocity to the Commission's own examination.

Conflicts of Interest of Investment Advisers

The Special Study Report discussed various situations where the nature of the advice given by investment advisers could be affected by consideration of their own interests. It particularly questioned the purchase of securities by an investment adviser for his own account shortly before recommending such securities, followed by a sale after the market price reflects the impact of the recommendation. This practice is known as "scalping."

With a view to identifying and possibly regulating conflicts-of-interest situations involving investment advisers, the Commission amended Rule 204-2 (a) of the Investment Advisers Act of 1940 to require investment advisers to maintain records concerning transactions in which they or their "advisory representatives" (as that term is defined in the rule) have a beneficial interest.

In announcing the amendment, the Commission pointed out that an investment adviser is a fiduciary, and as such owes his clients undivided loyalty, should not engage in any activity in conflict with the interest of clients, and should take the steps reasonably necessary to fulfill his fiduciary obligations. It referred to the holding by the United States Supreme Court in SEC v. Capital Gains Research Bureau, 375 U.S. 180 (1963), that "scalping" by an investment adviser violates the anti-fraud provisions of Sections 206 (1) and (2) of the Advisers Act unless appropriately disclosed. The Commission has considered whether it should adopt a rule designed to prevent "scalping" by prohibiting specified transactions by investment advisers and their associates in securities recommended by them. It is expected that the new record-keeping requirement will assist the Commission in determining whether such a rule is necessary and if so, what its nature and scope should be. In addition, the reports furnished to investment advisers by their "advisory representatives" should provide the investment advisers with valuable information on the basis of which they may establish appropriate internal controls over representatives' trading.

New Building

The Commission completed its move into new quarters in June 1966 The building is conveniently located at 500 North Capitol Street, facing Union Station Plaza.

For the first time in its 32-year history, the Commission's Headquarters Office is housed in a single modern office building with suitable facilities and accommodations. This

consolidation of the Washington staff (including the Washington Regional Office) into one building will contribute to a more orderly and efficient conduct of the Commission's business. Coincident with the move, the Commission undertook to improve its service to the public. For example, better facilities are now available for the public's examination of corporate and other reports on file with the Commission. In addition, new and improved telephone facilities have been installed which will permit direct transfers of incoming telephone calls without rerouting through the master switchboard. The Commission will continue to press forward in every possible way to make improvements in its service to the public. In a message sent to the dedication ceremonies, President Johnson said:

"It gives me great pleasure to congratulate you on the attainment of a much-needed goal -- the efficient and attractive quarters being dedicated today.

"For many years the Securities and Exchange Commission has labored under the handicap of a series of so-called "temporary" buildings. I am glad that we could finally obtain this new and more pleasant working environment for your dedicated public servants.

"The modern facilities now at your disposal will undoubtedly result in even better service to the public and the securities industry. A valuable by-product of the new SEC building deserves mention. The important Washington gateway at Union Station, adjacent to the Capitol, should add to an impressive first view for our visitors arriving by rail. The SEC building significantly improves the vista on this spacious plaza. It makes a notable contribution to our efforts to create a more beautiful Washington. I share the pride of the Commission and its staff in your new home and you have my best wishes for the future."

Installation and Use of Electronic Data-Processing Equipment

In May 1966, following extensive studies and preparatory work, a computer was delivered to the Commission in its new building. The equipment is being used for a variety of regulatory, enforcement, statistical and house-keeping uses.

In one important application of EDP, the Commission has begun operation of an integrated regulatory and enforcement information system which combines information as to names, numbers and descriptions previously contained only in a number of separate indexes. The new system will permit a speedier, more accurate and more comprehensive verification of information in incoming documents against information already on file. It will also be used to provide supervisory personnel with meaningful information about the large number of documents which are under examination at any given time. A second important application of automation is in the area of surveillance of the over-the-counter securities markets on a comprehensive basis which was not feasible under the former manual methods. The computer is programmed to identify unusual price movements or dealer interest, securities which are quoted in the inter-dealer market after lengthy absence, and those in which there are "special arrangements" among broker-dealers. If a

security is identified for any of these reasons, the system will print out the security and the dealers involved, permitting the rapid detection of potentially troublesome areas.

The computer is also being used to analyze various data relating to the securities industry. These analyses will materially assist the Commission in carrying out its regulatory functions. EDP applications planned for the future include the development and programming of a system for legal and accounting research and the expansion of the integrated regulatory and enforcement system to provide for EDP surveillance of security holdings and transactions required to be reported by corporate insiders.

PART II
OPERATION OF THE SECURITIES ACTS AMENDMENTS OF 1964

Extension of Disclosure Requirements to Over-the-Counter Securities

Section 12 (g) of the 1964 amendments extended to many securities traded in the over-the-counter markets the registration, periodic reporting, proxy solicitation and insider reporting and trading provisions of the Exchange Act previously applicable to securities listed on a national securities exchange. This Section requires a company with total assets exceeding 1 million dollars and a class of non-exempt equity securities not previously registered under Section 12 which is held of record by 500 or more persons to register those securities by filing a registration statement.

During the fiscal year, 676 registration statements were filed under Section 12 (g). From the enactment of the 1964 amendments through June 30, 1966, 2,184 registration statements were filed under this Section. Six of these statements were withdrawn before they had become effective upon the determination that they were not required to be filed under the Act. Sixteen registrations were terminated pursuant to Section 12 (g) (4) because the number of shareholders fell under 300.

Of the 2,184 registration statements filed under Section 12 (g), 1,310 were filed by issuers already subject to the reporting requirements of Sections 13 or 15 (d) of the Act. Of this latter figure 106 registration statements (78 in fiscal 1965 and 28 in fiscal 1966) were filed by issuers with another security registered on a national securities exchange under Section 12 of the Act, and 1,204 were filed by issuers subject to the reporting requirements of Section 15 (d) (851 during fiscal 1965 and 353 during fiscal 1966). These latter companies had not been subject to the proxy solicitation and insider reporting and trading provisions of Sections 14 and 16 of the Exchange Act. The remaining 868 issuers which filed registration statements had not been subject to any of the disclosure or insider trading provisions and became subject to them through registration.

During the fiscal year, the Commission granted 250 extensions of time for filing, including more than one request by some issuers. A majority of these requests was based on the difficulties encountered by independent accountants in preparing certified financial statements within the prescribed time when prior financial statements had not been certified.

During the fiscal year, 1,304 definitive proxy statements were filed pursuant to Regulation 14A by issuers with securities registered under Section 12 (g). In addition, 19 out of 37 proxy contests occurring during the year which were subject to Regulation 14A involved securities registered under Section 12 (g).

As a further consequence of Section 12 (g), there was a great increase in the number of ownership reports filed this year pursuant to Section 16 (a).

Section 14 (c) of the Exchange Act, added by the 1964 amendments, requires issuers of securities registered under Section 12 to file with the Commission and transmit to security holders from whom proxies are not solicited for a meeting of stockholders an information statement containing information comparable to that which would be furnished in proxy material if proxies were solicited. During the fiscal year, the Commission adopted Regulation 14C, setting forth the requirements for this information statement. In the case of an annual meeting the issuer is also required to transmit to security holders an annual report including financial statements certified by independent public or certified public accountants, similar to the annual report required of issuers which solicit proxies.

Rule 14c-7 of the new regulation provides that if the issuer knows that securities of any class entitled to vote at a meeting are held of record by a broker, dealer, bank or voting trustee, or their nominees, the issuer must inquire whether other persons are beneficial owners of such securities and must furnish the record holder with enough copies of the information statement and annual report to enable the record holder to send copies to the beneficial owners. The issuer must pay the reasonable expenses of the record holders in transmitting this material. This latter provision is similar to Rule 14a-2 (b) of the proxy rules.

Regulation 14C applied to any meeting of security holders held on or after March 15, 1966. During the fiscal year, 53 information statements in definitive form were filed with the Commission pursuant to the regulation.

Section 12 (i) provides, in effect, that for securities issued by banks, the responsibility for administering and enforcing Sections 12, 13, 14 (a), 14 (c) and 16 of the Exchange Act is vested in the Comptroller of the Currency, the Board of Governors of the Federal Reserve System and the Federal Deposit Insurance Corporation, depending on which agency has primary supervisory jurisdiction over a particular bank. The Commission understands that information regarding the operation of the Securities Acts Amendments of 1964 with

respect to banks under the supervision of these agencies is discussed in their respective annual reports or is otherwise available from them.

Exemptions From Registration

Section 12 (h) of the Act authorizes the Commission, either by rules and regulations or by order upon application of an interested person, to grant a complete or partial exemption from the provisions of Sections 12 (g), 13, 14, 15 (d), or 16 if the Commission finds that because of the number of public investors, the amount of trading interest in the securities, the nature and extent of the activities of the issuer, the income or assets of the issuer, or otherwise, the exemption is not inconsistent with the public interest or the protection of investors.

During the fiscal year, 22 applications for complete or partial exemptions were filed; 21 applications filed during the prior year were pending. Of these 43 applications, 22 were granted,4 2 were denied, 7 were withdrawn, and 12 were pending at the end of the year. Exemptions were granted for a wide variety of reasons. Several mutual or cooperative organizations which did not meet all of the technical criteria of Section 12 (g) (2) (F) for exclusion from registration under Section 12 (g) were granted complete exemptions. Several issuers which were in the process of liquidation or of taking steps which would shortly terminate the public ownership of their securities, and whose registrations would therefore be shortly terminated were also exempted completely. Exemptions from Section 14 (c) only were granted to several other issuers, only a small percentage of whose securities were held by the public and whose operations consisted solely of the receipt of rentals for property leased to affiliates.

Section 12 (g) (2) exempts various types of securities from the registration requirements of Section 12 (g) including the securities of an insurance company if (1) the company is required to and does file an annual statement conforming to that prescribed by the National Association of Insurance Commissioners ("NAIC") with the insurance regulatory authority of its domiciliary state; (2) the company is regulated in the solicitation of proxies as prescribed by the NAIC; and (3) after July 1, 1966, the purchase and sale of securities issued by the company are subject to reporting and trading regulations by its domiciliary state in substantially the same manner as provided by Section 16 of the Act.

The NAIC has prescribed a uniform annual reporting form which has been adopted in every State and the District of Columbia as the required form for insurance companies. As part of that form, the NAIC has developed a "stockholders' information supplement" to determine whether the company has furnished its stockholders with information substantially equivalent to that which the Commission would require under its periodic reporting requirements and proxy rules. The Commission has been informed that, as of the close of the fiscal year, the insurance regulatory agencies of every State and the District of Columbia had adopted rules and regulations requiring companies within their

jurisdiction to file the supplement and any future revisions, and to comply with the proxy solicitation practices referred to therein. Many states also had enacted legislation specifically authorizing the adoption of such rules and regulations.

The NAIC also supported enactment of a model insider trading statute affording investor protections comparable to those of Section 16 of the Exchange Act. As of August 15, 1966, all of the States and the District of Columbia had passed such legislation.

Section 12 (g) (3) authorizes the Commission to exempt foreign securities and certificates of deposit for such securities from the registration requirements of Section 12 (g) if it finds that such action is in the public interest and is consistent with the protection of investors. Rule 12g3-1, adopted on September 15, 1964, exempted all foreign securities from registration until November 30, 1965.5 This exemption afforded the Commission time to study the problems of the registration of foreign securities traded in the over-the-counter market. On November 16, 1965, the Commission published for public comment proposed rules and forms for the registration of foreign securities under Section 12 (g).

The Commission received many comments on the proposed rules, including many from persons and companies who would be directly affected by them and from representatives of foreign governments. Most of those who submitted comments suggested that the application of the requirements of the Exchange Act to foreign issuers which were neither listing shares on a United States securities exchange nor offering new shares in this country would be improper under international law. A number of comments indicated that in particular areas there would be technical difficulties in superimposing the requirements of the proposed rules on existing law to which issuers were subject in their country of incorporation.

After considering the comments, the Commission further postponed the application of Section 12 (g) to foreign issuers, by amending Rule 12g3-1 to extend the exemption from registration to November 30, 1966. During the further period of exemption, the Commission continued its study of the adequacy of information now furnished by foreign issuers, the development and effects of the changing foreign law in this field, and the need for technical changes in the proposed rules because of foreign laws and practices. As of November 30, 1966, the exemption had not been extended further. The earliest date by which a foreign issuer would be required to register, if the Commission did not grant a further exemption, is 120 days after its first fiscal year ending after November 30, 1966.

To assist the Commission during the further exemption, and to provide information as promptly as possible to American investors, the Commission asked foreign issuers to furnish the Commission with certain information if they had in excess of $1 million of total assets and a class of equity securities with 500 or more holders (at least 300 of which are residents of the United States) at the end of a fiscal year ending after November 30, 1965. The information requested was that which issuers were required to publish under foreign law or to furnish to foreign stock exchanges, or which they

distributed to their own security holders. The information so furnished would be available for public inspection.

On August 10, 1966, the Commission published a list of 80 foreign issuers which had furnished information voluntarily and 32 issuers which had not done so. The Commission will publish additional lists as additional companies furnish information. The Commission believes that these lists will be useful to brokers and dealers in making recommendations to their customers concerning the securities of foreign companies.

Proposed Definitions Under the "Market-Maker" Exemption From Insider Trading Provisions

Section 16 (d) of the Exchange Act, added by the 1964 amendments, exempts market-making transactions by broker-dealers from the profit recovery provisions of Section 16 (b) and the "short sale" and "sale against the box" provisions of Section 16 (c). On June 16, 1966, the Commission proposed for public comment a new Rule 16d-1 defining certain terms in Section 16 (d) and specifying conditions for the availability of the exemption.

The proposed rule would define the term "securities held in an investment account" as used in Section 16 (d) to mean securities which a dealer has identified on his records as being held in an investment account, securities acquired in other than market-making transactions and securities held by the dealer more than 5 business days after the dealer ceases to maintain a market in the securities. The acquisition of these securities would not be exempt from Section 16 (b) even though made in a market-making transaction. The term "transactions made in the ordinary course of business and incident to the establishment or maintenance of a primary or secondary market" (referred to in the rule as "market-making transactions") would be defined to mean both retail and inter-dealer transactions in securities which are sold, or acquired and held for sale, in the ordinary course of business and incident to the establishment or maintenance of a market. The rule would require as a basis for exemption that the dealer maintain a continuous inter-dealer market in the securities on each business day for a period of at least 45 consecutive calendar days, including the day of the transaction for which exemption is claimed. At the close of the fiscal year, the Commission was considering the comments and suggestions which it had received.

Disciplinary Action Against Broker-Dealers and Their Associated Persons

The 1964 amendments added several important provisions to Section 15 of the Exchange Act concerning disciplinary action against brokers and dealers and persons associated with them. For the first time, the Commission was authorized to proceed directly against and impose sanctions on individuals associated with broker-dealer firms. These sanctions include a suspension or a bar from being associated with a broker-dealer. The sanctions which the Commission may impose against broker-dealers were expanded to permit

censure and suspension of registration for up to 12 months. The statutory disqualifications from being registered as or associated with a broker-dealer were expanded to include additional types of injunctions, convictions and violations.

During fiscal 1966, the Commission applied the new provisions in many instances. It instituted four proceedings solely against individuals associated with broker-dealers. Another such proceeding was pending at the start of the fiscal year. During the year, a respondent in one of the above proceedings was barred from further association with a broker-dealer. In proceedings in which broker-dealers as well as certain of their associated persons were named as respondents, 67 individuals were barred from further association with a broker or dealer, and 9 others were suspended from such association for varying periods of time. The Commission also suspended the registrations of six broker-dealer firms.

Regulation of Broker-Dealers Who Are Not Members of Registered Securities Associations

Prior to the 1964 amendments, broker-dealers registered with the Commission who were not members of the National Association of Securities Dealers, Inc. (NASD), or one of the principal exchanges, were not subject to any comprehensive regulation concerning qualifications, experience in the securities business, or fair business practices. A major objective of the amendments was "to insure that the Commission has the necessary authority to provide regulation of non-member brokers and dealers comparable to that imposed by (self-regulatory) associations on their membership, including the requirement that these non-member brokers and dealers pay fees which will compensate the Commission for this additional regulation."

New subsections (8), (9), and (10) of Section 15 (b) of the Exchange Act authorize the Commission to adopt rules and regulations prescribing standards of training, experience and other qualifications for such brokers and dealers and persons associated with them, as well as to adopt rules and regulations for non-member broker-dealers designed to promote just and equitable principles of trade, to provide safeguards against unreasonable profits or unreasonable rates of commissions or other charges, and in general to protect investors and the public interest and to remove impediments to and perfect the mechanism of a free and open market.

During the past fiscal year, the Commission continued to implement these provisions. In September 1965, the Commission adopted Rule 15b8-1 which, among other things, established qualification requirements for registered broker-dealers who do an over-the-counter business and who are not members of a registered securities association, and for their principals, salesmen and other associated persons. Subject to certain exemptions, every associated person engaged directly or indirectly in securities activities must now successfully complete a qualifications examination, and broker-dealers subject to the rule must file a personnel form for every such associated person with the Commission.

In January 1966, the Commission's general securities examination, administered by the NASD, was given for the first time. The examination covers a broad range of securities subjects, including corporate structure, financial statements and accounting theory, investment companies, the securities laws, details of underwriting, trading and distributions, and other Federal rules and regulations such as Regulations "T" and "U" of the Federal Reserve Board. By the end of the fiscal year, 3,315 examinations had been given in over 70 testing centers in the United States and Puerto Rico. The examination was first given in United States consulates abroad in August 1966.

An associated person may also satisfy the examination requirement by passing an examination which the Commission deems a satisfactory alternative to its own. Such examinations include, thus far, those given by the NASD, certain of the national securities exchanges, many States, and the NAIC (in connection with variable annuities).

The Commission reviewed and processed more than 22,000 personnel forms received from approximately 450 non-member broker-dealers during the year. The Commission will use the information in these forms to formulate further qualification standards for non-member broker-dealers and associated persons. The data is also being coded and tabulated for a statistical study of non-member broker-dealers.

In June 1966, the Commission adopted Rule 15b8-2, which among other things established assessments for fiscal 1966. The assessments apply to broker-dealers who had been registered with the Commission for at least 45 days as of June 30, 1966, and who were not members of a registered securities association on that date, as well as to broker-dealers who, although members of a registered securities association on August 1, 1966 (the effective date of the rule), were for at least 45 days during fiscal 1966 both registered with the Commission and not members of such association. The rule requires the filing of an assessment form and payment of a base fee for each such broker-dealer, and imposes an additional levy for each associated person and each office of the broker-dealer.

The rule also requires broker-dealers registering with the Commission after the effective date of the rule, who do not become members of a registered securities association within 45 days after their registration with the Commission, to pay a fee of $150. In addition, there is a $25 fee for each personnel form filed after August 1, 1966, except those forms filed for persons for whom such a form had previously been filed by the firm and for persons who conduct all their securities activities outside the United States and do not deal with any United States residents or nationals.

The rule exempts broker-dealers who are members of a national securities exchange if they do not carry customers' accounts and if their annual gross income derived from over-the-counter business is no more than $1,000. This exemption applies mainly to exchange specialists and other floor members who occasionally introduce accounts to other members.

A program for the inspection of non-member broker-dealers has been formulated, and the first inspections were conducted in August 1966. In addition, the Commission's staff has drafted rules under Section 15 (b) (10) concerning the business conduct and selling practices of broker-dealers, and additional rules concerning advertising and sales literature are being prepared.

Summary Suspension of Over-the-Counter Trading

Section 15 (c) (5) of the 1964 amendments authorizes the Commission to suspend over-the-counter trading in any security (except an exempted security) summarily for 10 days if the Commission believes the public interest and protection of investors so require. Broker-dealers are prohibited from trading in any such security during the period of suspension. This provision is a counterpart to Section 19 (a) (4) which provides for summary suspension of trading in securities listed on a national securities exchange.

During the 1966 fiscal year, the Commission temporarily banned trading in five over-the-counter securities. In three of these cases, the Commission suspended trading when it learned of information not generally known to the securities community and investors which indicated that there were substantial questions concerning the financial condition or business operations of the companies involved. The suspensions were ordered pending clarification and adequate public dissemination of information concerning these matters.

The Commission suspended trading in the securities of two other issuers concurrently with the institution of court action to enjoin violations of the Federal securities laws in the offer and sale of such securities. These suspensions were imposed to permit public disclosure of the information developed and the steps taken by the Commission in the course of its investigations of the violations.

The Commission also acted under Section 15 (c) (5) in several instances where it ordered suspensions at the same time under Section 19 (a) (4) for securities traded on national securities exchanges. In these cases, the Commission found it necessary to suspend over-the-counter trading to prevent circumvention of the exchange suspension.

Changes in NASD Regulations

Pursuant to additional powers granted the NASD under the 1964 amendments, the Association amended its By-Laws and Rules of Fail-Practice in September 1965 to establish further qualification requirements and standards for members and persons associated with members, as well as to expand the Association's bars to eligibility for membership. These new regulations also permit the Association in disciplinary actions to proceed directly against associated persons without necessarily joining the member firm.

PART III
LEGISLATIVE ACTIVITIES

On October 22, 1965 the President signed Public Law 89-289, amending the Securities Act of 1933. This legislation, proposed by the Commission, increased the fees payable for the registration of securities under the Securities Act from 1/100 of 1 percent of the maximum aggregate offering price of the securities to be offered, or 10 cents per $1000, with a minimum fee of $25, to 1/50 of 1 percent, or 20 cents per $1000, with a minimum of $100. As a result, the Commission will be able to recover more of the costs of administration of the Federal securities laws.

Chairman Cohen testified on behalf of the legislation on September 14, 1965, before the Committee on Interstate and Foreign Commerce, House of Representatives, and oil September 22, 1965, before the Subcommittee on Securities of the Committee on Banking and Currency, United States Senate.

On March 11, 1966, Chairman Cohen appeared before the Subcommittee on Financial Institutions of the Committee on Banking and Currency, United States Senate, and submitted a written statement in opposition to S. 2704, a bill to provide for the regulation of collective investment funds maintained by banks. Under the bill, interests in such funds would be excluded from the definition of "security" in the Securities Act and the Securities Exchange Act, and the funds would be excluded from the definition of "investment company" in the Investment Company Act. The Chairman stated that the Commission objected to the bill principally because it was special legislation which would permit banks to offer to the public collective investment management similar to that offered by mutual funds but without the proven safeguards which the Securities Act and the Investment Company Act afford to investors.

Chairman Cohen also testified on June 22, 1966, before the Subcommittee on Securities of the Committee on Banking and Currency, United States Senate, concerning S. 2672, a bill to regulate the interstate sale of undeveloped subdivision lots. Among other things, the bill, which follows the pattern of the Securities Act, would require a real estate developer to file with the Commission a registration statement making specified disclosures if he subdivided land into 25 or more units or interests for the purpose of sale or lease as part of a common promotional plan, and to furnish a prospectus to a prospective purchaser or lessee at least 48 hours before a contract was entered into. The bill also contains provisions designed to prevent and punish fraud. The Chairman pointed out that administration of the bill by the Commission would to some extent divert its attention from its primary function, the regulation of the securities markets. He stated, however, that if the bill were enacted into law, the Commission would do its best to carry out the legislative purpose effectively and economically. The Chairman also submitted for the record an analysis of the bill and certain suggestions for amendment.

The Commission's General Counsel, Philip A. Loomis, Jr., testified on April 4, 1966, before the Subcommittee on Domestic Marketing and Consumer Relations of the Committee on Agriculture, House of Representatives, with respect to H.R. 11788, a bill to amend the Commodity Exchange Act.

During the fiscal year the Commission and its staff analyzed or commented on 43 bills and other legislative matters referred by various committees of the Senate and House of Representatives, individual members of Congress, the Bureau of the Budget and other Federal agencies.

PART IV
ADMINISTRATION OF THE SECURITIES ACT OF 1933

The Securities Act of 1933 is designed to provide disclosure to investors of material facts concerning securities publicly offered for sale by the use of the mails or instrumentalities of interstate commerce, either by an issuing company or by any person in a control relationship to such company, and to prevent misrepresentation, deceit, or other fraudulent practices in the sale of securities generally. Disclosure is obtained by requiring the issuer of such securities to file a registration statement with the Commission which includes a prospectus containing significant financial and other information about the issuer and the offering. The registration statement is available for public inspection as soon as it is filed. Although the securities may be offered for sale as soon as the registration statement has been filed, actual sales may not be made until the registration statement has become effective. A copy of the prospectus must be furnished to each purchaser at or before the sale or delivery of securities in order to provide him with an opportunity to evaluate such securities and make an informed investment decision. The issuer and the underwriter are responsible for the contents of the registration statement. The Commission has no authority to control the nature or quality of a security to be offered for public sale or to pass upon its merits or the terms of its distribution. Its action in permitting a registration statement to become effective does not constitute approval of the securities, and any representation to the contrary to a prospective purchaser violates Section 23 of the Act.

DESCRIPTION OF THE REGISTRATION PROCESS

Registration Statement and Prospectus

Registration of any security proposed to be publicly offered may be effected by filing with the Commission a registration statement on the applicable form containing the prescribed disclosure. Generally speaking, a registration statement relating to securities issued by a corporation or other private issuer must contain the information specified in

Schedule A of the Act, while a statement relating to securities issued by a foreign government must include the information specified in Schedule B. Securities issued by the United States, by a state, or by any political subdivision of a state are exempt from the registration provisions of the Act. The Act empowers the Commission to classify issues, issuers and prospectuses, to prescribe appropriate forms, and to increase, or in certain instances vary or diminish, the particular items of information required to be disclosed as the Commission deems appropriate in the public interest or for the protection of investors. To facilitate the registration of securities by different types of issuing companies, the Commission has prepared special registration forms which vary in their disclosure requirements so as to provide maximum disclosure of the essential facts pertinent in a given type of case while at the same time reducing the burden and expense of compliance with the law.

In general, the registration statement of an issuer other than a foreign government must disclose such matters as the names of persons who participate in the management or control of the issuer's business; the security holdings and remuneration of such persons; the general character of the business, its capital structure, past history and earnings; underwriters' commissions; payments to promoters made within 2 years or intended to be made; the interest of directors, officers and principal stockholders in material transactions with the issuer; pending legal proceedings; and the purposes to which the proceeds of the offering are to be applied, and must include financial statements certified by Independent accountants. The registration statement of a foreign government contains information concerning the purposes for which the proceeds of the offering are to be used, the natural and industrial resources of the issuer, its revenues, obligations and expenses, the underwriting and distribution of the securities being registered, and other material matters. The prospectus constitutes a part of the registration statement and contains the more important of the required disclosures.

Examination Procedure

Registration statements are examined by the Commission's staff for compliance with the standards of adequate and accurate disclosure. This examination is primarily the responsibility of the Division of Corporation Finance. Statements filed by investment companies registered under the Investment Company Act of 1940 are examined by the Division of Corporate Regulation. If it appears that a statement does not conform in material respects with the applicable requirements, the registrant is visually notified by a letter of comment and is afforded an opportunity to file correcting or clarifying amendments. The Commission also has the power, after notice and opportunity for hearing, to issue an order suspending the effectiveness of a registration statement if it finds that material representations are misleading inaccurate or incomplete. In certain instances, such as where the deficiencies in a registration statement appear to stem from careless disregard of applicable requirements or from a deliberate attempt to conceal or mislead, a letter of comment is not sent and the Commission either institutes an investigation to determine whether "stop-order" proceedings should be instituted or

immediately institutes such proceedings. Information regarding the exercise of the "stop-order" power during fiscal year 1966 appears below under the heading "Stop-Order Proceedings."

Time Required to Complete Registration

The Commission's staff endeavors to complete its examination of registration statements in as short a time as possible. The Act provides that a registration statement shall become effective on the 20th day after it is filed (or on the 20th day after the filing of any amendment thereto). Since most registration statements require one or more amendments, they usually do not become effective until some time after the original 20-day period. The period between filing and effective date is intended to afford investors an opportunity to become familiar with the proposed offering through the dissemination of the preliminary form of prospectus. The Commission can accelerate the effective date so as to shorten the 20-day waiting period, taking into account the adequacy of the information respecting the issuer theretofore available to the public, the facility with which the facts about the offering can be understood, the public interest and the protection of investors. The note to Rule 460 under the Act lists some of the more common situations in which the Commission considers that the statute generally requires it to deny acceleration.

The median number of calendar days from the date of the original filing to the effective date for the 1,280 registration statements that became effective during the 1966 fiscal year was 38, compared, with 36 days for 1,097 registration statements in fiscal year 1965 and 36 days for 960 registration statements in fiscal year 1964.

The following table shows by months during the 1966 fiscal year the number of calendar days elapsed during each of the three principal stages of the registration process for the median registration statement, the total elapsed time and the number of registration statements which became effective.

[table omitted]

VOLUME OF SECURITIES REGISTERED

During the fiscal year 1966, 1,523 registrations of securities in the amount of $30.1 billion became effective under the Securities Act of 1933. The number of statements was the highest since the year ended June 1962, and the dollar amount of registrations was the largest on record. The large volume of issues reflected the general expansion in the economy during the period and the sharply increased need for funds by business. The chart on page 25 shows the number and dollar amounts of registrations from 1935 to 1966.

The figures for 1966 include all registrations which became effective including secondary distributions and securities registered for other than cash sale, such as issues exchanged for other securities, and securities reserved for conversion. Of the dollar amount of securities registered in 1966, 85 percent was for account of issuer for cash sale, 8 percent for account of issuer for other than cash sale, and nearly 7 percent for account of others, as shown below.

[table omitted]

The amount of securities offered for cash for account of issuer, $25.7 billion, represented an increase of $11 billion, or 75 percent, over the previous year. Registration of new common stock issues aggregated $18.2 billion, $7.6 billion more than in the 1965 fiscal period, reflecting the continuing increase of registrations of investment company issues which aggregated a record $12.4 billion. The amount of investment company issues was almost double that of the preceding year. Registration of new bonds, notes and debentures increased 90 percent from the previous year and accounted for $7.1 billion of the 1966 volume. Preferred stock issues amounted to $445 million. Appendix Table 1 shows the number of statements which became effective and total amounts registered for each of the fiscal years 1935 through 1966, and contains a classification by type of security of issues to be offered for cash sale on behalf of the issuer during those years. More detailed information for 1966 is given in Appendix Table 2.

Corporate issues scheduled for immediate cash sale totaled almost $8.8 billion, an increase of $3.4 billion over the previous year. Electric, gas and water companies registered $3.0 billion of new issues, the largest amount for this group since 1958. Manufacturing company issues were next highest in volume, totaling $2.8 billion, the largest amount since 1961. Issues of communication companies amounted to $1.3 billion, almost double the amount registered in the previous year. Among the other industry groups, registration of financial and real estate issues totaled $1.0 billion, while trade, service, mining and other miscellaneous issues amounted to over $500 million. Registration of foreign government issues scheduled for immediate sale increased to $482 million from $303 million in the preceding year. In addition, one foreign government issue of $100 million was planned for offering on a continuous basis over a number of years.

The following table gives the distribution by industry of issues registered for account of issuer to be offered for cash sale during the last 3 fiscal years:

[table omitted]

Of the $8.8 billion expected from the immediate cash sale of corporate securities for the account of issuers in 1966, over 90 percent was designated for plant and equipment expenditures ($6.4 billion) and working capital ($1.5 billion). The total figure of $7.9 billion represented an increase of more than 50 percent over the corresponding figure for

fiscal 1965. The balance was to be used for retirement of securities and for other purposes including purchase of securities -and repayment of bank loans.

Registration of issues to be offered over an extended period amounted to $16.5 billion compared with $9.0 billion in 1965, the largest amount in any previous fiscal year. These issues are classified below:

[table omitted]

REGISTRATION STATEMENTS FILED

During the 1966 fiscal year, 1,697 registration statements were filed for offerings of securities aggregating $31.1 billion, as compared with 1,376 registration statements filed during the 1965 fiscal year for offerings amounting to $19.1 billion. This represents an increase of 23.2 percent in the number of statements filed and 62.5 percent in the dollar amount involved.

Of the 1,697 registration statements filed in the 1966 fiscal year, 422, or 25 percent, were filed by companies that had not previously filed registration statements under the Securities Act of 1933. Comparable figures for the 1965 and 1964 fiscal years were 458, or 33 percent, and 322, or 27 percent, respectively.

From the effective date of the Securities Act through June 30, 1966, a cumulative total of 27, 119 registration statements has been filed by 12,065 different issuers covering proposed offerings of securities aggregating over $308 billion.

The disposition of all registration statements filed under the Act to June 30, 1966 is summarized in the following table:

[table omitted]

The reasons given by registrants for requesting withdrawal of the 148 registration statements that were withdrawn during the 1966 fiscal year are shown in the following table:

[table omitted]

STOP ORDER PROCEEDINGS

Section 8 (d) of the Act provides that, if it appears to the Commission at any time that a registration statement contains an untrue statement of a material fact or omits to state any material fact required to be stated therein or necessary to make the statements therein not

misleading, the Commission may institute proceedings to determine whether a stop order suspending the effectiveness of the registration statement should be issued. Where such an order is issued, the offering cannot lawfully be made, or continued if it has already begun, until the registration statement has been amended to cure the deficiencies and the Commission has lifted the stop order.

At the beginning of the 1966 fiscal year, one stop order proceeding was pending. Four additional proceedings were instituted during the year, two were terminated (one through issuance of a stop order, and one through withdrawal of the registration statement pursuant to an offer of settlement), and three were pending at the end of the year.

The Wolf Corporation -- The registration statement of a cash flow real estate company was found materially false and misleading because it substantially overstated registrant's cash flow, net income and assets, and failed to disclose adequately registrant's relationship with affiliated persons. The Commission's opinion pointed out that the registrant's ability to maintain cash disbursements at the existing level was of paramount importance to prospective purchasers of its securities, and therefore a clear, uncomplicated statement of the basic facts relating to this issue was essential. Instead, registrant's presentation of its cash distribution policy and practices was highly deceptive. Registrant not only included in the term "cash available for distribution" amounts which represented anticipated income rather than cash, but included in such anticipated income substantial amounts of rent arrearages without disclosing any of the facts indicating that such arrearages were uncollectible. In view of registrant's affirmative representation that it believed such amounts would be paid in the future, the Commission found that a sophisticated investor -- and certainly an unsophisticated one -- could reasonably believe that the qualifying statement that "there is no assurance" that the rent arrearages would be paid was attributable to an excess of caution in the interest of full disclosure, and conclude that the uncollected (and uncollectible) rents were for all practical purposes equivalent to cash in hand. In fact, registrant had distributed to stockholders a sum which was more than twice as much as the cash actually derived from operations; the remainder apparently had come from funds borrowed for the purpose of making cash distributions to stockholders and thus maintaining a false appearance of a high level of cash available from operations.

Although the deficiencies were considered serious and extensive, the Commission did not issue a stop order but permitted the withdrawal of the registration statement pursuant to an offer of settlement. Registrant's offer provided that a stipulation correcting the principal deficiencies of the registration statement be included in the public record of the proceeding and that a written communication advising of the stop order proceeding be distributed to its stockholders and other persons to whom copies of the preliminary prospectus had been sent. In the Commission's view, this communication, which was to be reviewed by the Commission's staff prior to release, was sufficient to give adequate public notice of the dismal record of the abortive financial program and the deceptive disclosures in the prospectus. The factors that led to this conclusion were: (1) the

registration statement had never become effective; (2) none of the securities had been sold; (3) the proposed financing had been abandoned; and (4) the stipulation correcting the deficiencies was to become part of the public record.

EXAMINATIONS AND INVESTIGATIONS

The Commission is authorized by Section 8 (e) of the Act to make an examination in order to determine whether a stop order proceeding should be instituted under Section 8 (d), and in connection therewith is empowered to examine witnesses and require the production of pertinent documents. The Commission is also authorized by Section 20 (a) of the Act to make an investigation to determine whether any provision of the Act or any rule or regulation prescribed thereunder has been or is about to be violated. In appropriate cases, investigations are instituted under this Section as an expeditious means of determining whether a registration statement is false or misleading or omits to state any material fact. The following tabulation indicates the number of such examinations and investigations with which the Commission was concerned during the year:

[table omitted]

EXEMPTION FROM REGISTRATION OF SMALL ISSUES

The Commission is authorized under Section 3 (b) of the Securities Act to exempt, by its rules and regulations and subject to such terms and conditions as it may prescribe therein, any class of securities from registration under the Act, if it finds that enforcement of the registration provisions of the Act with respect to such securities is not necessary in the public interest and for the protection of investors because of the small amount involved or the limited character of the public offering. Only offerings not exceeding $300,000 may thus be exempted.

Acting under this authority, the Commission has adopted the following exemptive rules and regulations:

Rule 234: Exemption of first lien notes.

Rule 235: Exemption, of securities of cooperative housing corporations.

Rule 236: Exemption of shares offered in connection with certain transactions.

Regulation A: General exemption for United States and Canadian issues up to $300,000.

Regulation B: Exemption for fractional undivided interests in oil or gas rights up to $100,000.

Regulation F: Exemption for assessments on assessable stock and for assessable stock offered or sold to realize the amount of assessment thereon.

Under Section 3 (c) of the Securities Act, which was added by Section 307 (a) of the Small Business Investment Act of 1958, the Commission is authorized to adopt rules and regulations exempting securities issued by a company which is operating or proposes to operate as a small business investment company under the Small Business Investment Act. Acting pursuant to this authority, the Commission adopted Regulation E which exempts, subject to terms and conditions substantially similar to those contained in Regulation A, securities offerings not exceeding $300,000 by any small business investment company which is registered under the Investment Company Act of 1940.

Exemption from registration under Section 3 (b) or 3 (c) of the Act does not carry with it any exemption from the provisions of the Act prohibiting fraudulent conduct in the offer or sale of securities and imposing civil liability or criminal responsibility for such conduct.

Exempt Offerings Under Regulation A

Regulation A permits a company to obtain needed capital not in excess of $300,000 (including underwriting commissions) in any one year from a public offering of its securities without registration, provided specified conditions are met. These include the filing of a notification supplying basic information about the company with the Regional Office of the Commission in the region in which the company has its principal place of business, and the filing and use in the offering of an offering circular. However, an offering circular need not be filed or used in connection with an offering not in excess of $50,000 by a company with earnings in one of the last 2 years.

During the 1966 fiscal year, 410 notifications were filed under Regulation A, covering proposed offerings of $75,218,434, compared with 397 notifications covering proposed offerings of $77,367,235 in the 1965 fiscal year. Included in the 1966 total were 9 notifications covering stock offerings of $2,242,800 by companies engaged in the exploratory oil and gas business, 12 notifications with respect to offerings of $2, 190,224 by mining companies and 23 notifications covering offerings of $5,823,237 by companies featuring new inventions, products or processes.

The following table sets forth various features of the Regulation A offerings during the past 3 fiscal years:

[table omitted]

Reports of Sales

The Commission requires, within 30 days after the end of each 6-month period following the date of the original offering circular required by Rule 256, or the statement required by Rule 257, that the issuer or other person for whose account the securities are offered shall file a report containing specified information and that a final report shall be made upon completion or termination of the offering.

During the fiscal year 1966,864 Reports of Sales were filed reporting aggregate sales of $48,632,121.

Suspension of Exemption

Regulation A provides for the suspension of an exemption thereunder where, in general, the exemption is sought for securities for which the regulation provides no exemption or where the offering is not made in accordance with the terms and conditions of the regulation or with prescribed disclosure standards. Following the issuance of a temporary suspension order by the Commission, the respondent may request a hearing to determine whether the temporary suspension should be vacated or made permanent. If no hearing is requested within 30 days after the entry of the temporary suspension order and none is ordered by the Commission on its own motion, the temporary suspension order becomes permanent.

During the 1966 fiscal year, temporary suspension orders were issued in 6 cases, which, added to the 7 cases pending at the beginning of the fiscal year, resulted in a total of 13 cases for disposition. In 11 of these cases, the temporary suspension became permanent during the fiscal year: in 5 cases after hearing, in 5 by withdrawal of the request for hearing, and in 1 by lapse of time. Thus, there were 2 cases pending at the end of the fiscal year.

A decision of particular interest rendered by the Commission during the year in a Regulation A suspension proceeding was Del Consolidated Industries, Inc. In that case the Commission found that the offering circular filed by the issuer, which had been organized to engage in oil, gas and mining operations, contained materially misleading statements.

The introductory statement of the circular represented that the issuer had an option to acquire certain properties, including "working interests in four proven oil leases" in New Mexico, "consisting of four wells which produced approximately 15,000 barrels of oil in 1961," and that the properties were more fully described in the section "Business and Property." The introductory statement did not disclose that the options covered substantially less than the entire working interests in the leases. That fact was disclosed only in the "Business and Property" section, six pages later in the circular, following statistics regarding the production applicable to the entire working interests.

The Commission found that the misleading implication in the introductory statement that the option covered the entire working interests was not cured by the subsequent description. The Commission pointed out that even though an offering circular contains all of the essential facts, it still may not satisfy the disclosure requirements if the facts are not presented so clearly that they will be plainly evident to the ordinary investor. The Commission stated that the burden should not be placed on the investor to examine the offering circular for qualifying language to counteract the misleading nature of a statement in the introductory material which does its damage in its initial effect on the prospective investor.

The issuer requested that the temporary suspension order be vacated, asserting that it had abandoned plans for the proposed offering and that it had not been guilty of bad faith. However, the Commission, affirming the recommendation of the hearing examiner, concluded that the suspension should be made permanent, since it was satisfied that the issuer did not make "a diligent and careful effort" to make an accurate and adequate filing.

Exempt Offerings Under Regulation B

During the fiscal year ended June 30, 1966, 235 offering sheets and 302 amendments thereto were filed pursuant to Regulation B and were examined by the Oil and Gas Section of the Commission's Division of Corporation Finance. During the 1965 and 1964 fiscal years, 173 and 242 offering sheets, respectively, were filed. The following table indicates the nature and number of Commission orders issued in connection with such filings during the fiscal years 1964-66. The balance of the offering sheets filed became effective without order.

[table omitted]

Reports of sales -- The Commission requires persons offering securities under Regulation B to file reports of the actual sales made pursuant to that regulation. These reports aid the Commission in determining whether violations of law have occurred in the marketing of such securities. The following table shows the number of sales reports filed under Regulation B during the past 3 fiscal years and the aggregate dollar amount of sales during each of such fiscal years.

[table omitted]

Exempt Offerings Under Regulation E

Regulation E provides a conditional exemption from registration under the Securities Act for securities of small business investment companies which are licensed under the Small Business Investment Act of 1958 or which have received the preliminary approval of the Small Business Administration and have been notified by the Administration that they

may submit an application for such a license. As has been noted, the terms and conditions of the exemption are substantially similar to those provided by Regulation A. One notification was filed under Regulation E during the 1966 fiscal year for an offering of securities aggregating $100,000, which was pending at the end of the year.

Exempt Offerings Under Regulation F

Regulation F provides an exemption for assessments levied upon assessable stock and for delinquent assessment sales in amounts not exceeding $300,000 in any one year. It requires the filing of a simple notification giving brief information with respect to the issuer, its management, principal security holders, recent and proposed assessments and other security issues. The regulation requires a company to send to its stockholders, or otherwise publish, a statement of the purposes for which the proceeds of the assessment are proposed to be used. Copies of any other sales literature used in connection with the assessment must be filed. Like Regulation A, Regulation F provides for the suspension of an exemption thereunder where the regulation provides no exemption or where the offering is not made in accordance with the terms and conditions of the regulation or in accordance with prescribed disclosure standards.

During the 1966 fiscal year, 21 notifications were filed under Regulation F, covering assessments of $486,231. These notifications were filed in three of the nine regional offices of the Commission: Denver, San Francisco and Seattle. Underwriters were not employed in any of the Regulation F assessments. No Regulation F exemptions were suspended during the fiscal year.

REVISION OF RULES, REGULATIONS AND FORMS

Amendments to Rule 416

During the fiscal year, the Commission published for comment a proposal to amend Rule 416 relating to the coverage by a registration statement of certain securities issued to prevent dilution as a result of stock splits and stock dividends. After consideration of the comments received, the Commission adopted the proposed amendments with certain changes. The former Rule 416 has been designated Rule 416 (a), and concerns the coverage of securities offered or issued pursuant to anti-dilution provisions to holders of warrants, options, convertible securities, or similar rights to purchase securities, upon exercise of their rights. Rule 416 (b) broadens the scope of the former rule by extending the coverage of a registration statement to additional securities issued pursuant to a split of a class of securities which includes undistributed securities covered by the statement or pursuant to a dividend declared on and payable in securities of such class, where there are no applicable anti-dilution provisions. The rule also provides that when all the securities of a class which includes undistributed registered securities are combined by a reverse

split into a lesser number of shares, the amount of undistributed securities of such class covered by the registration statement shall be proportionately reduced.

Amendment of Rules and Forms Relating to Registration Fees

Part III of this Report discusses the statutory increase in the fees payable for the registration of securities. During the fiscal year the Commission amended Rules 457 and 458 and Forms D-1, D-1A and S-6, all of which refer to the required filing fee, to conform to the statutory changes. At the same time the Commission adopted additional amendments to Rule 457 to clarify the rule and to incorporate certain recurring administrative interpretations concerning the computation of filing fees. The rule sets forth the method of calculating fees in various situations in which the maximum aggregate offering price is based on fluctuating factors, such as market price or underlying asset values, or is otherwise uncertain at the time of filing.

In order to incorporate all provisions relating to the calculation of filing fees into one rule, the calculation provisions contained in Forms S-8 and S-12 were transferred to Rule 457, calculation provisions in Forms D-1, D-1 A and S-6 which were duplicated in Rule 457 were deleted from those Forms, and additional amendments of Rule 457 relating to the calculation of filing fees in connection with the registration of stock pursuant to certain employee stock options were adopted.

Withdrawal of Proposed Amendments of Rule 485

During the fiscal year, the Commission, after consideration of the comments received, withdrew proposed amendments of Rule 485. That rule prescribes the procedure for obtaining confidential treatment of material contracts.

Adoption of Form S-13

The Commission adopted a new Form S-13 for the registration of voting trust certificates, replacing Form F-1. The disclosure requirements correspond to those in the recently revised Form 16, the form for the registration of voting trust certificates pursuant to Section 12 of the Securities Exchange Act of 1934.

PART V
ADMINISTRATION OF THE SECURITIES EXCHANGE ACT OF 1934

The Securities Exchange Act of 1934, as amended by the Securities Acts Amendments of 1964, provides for the registration and regulation of securities exchanges, the registration of securities listed on such exchanges and, under new Section 12 (g), the registration of securities traded over the counter where the issuers of such securities have total assets in

excess of $1 million and the securities constitute a class of equity securities held of record by at least 500 persons (until July 1, 1966, the minimum number was 750). It establishes, for issuers of securities registered under the Act, financial and other reporting requirements and regulation of proxy solicitations and, for directors, officers and principal security holders of such issuers, reporting requirements and restrictions on trading in the securities of their companies. The Act also provides for the registration and regulation of national securities associations and of brokers and dealers doing business in the over-the-counter markets, contains provisions designed to prevent fraudulent, deceptive and manipulative acts and practices on the exchanges and in the over-the-counter markets and authorizes the Board of Governors of the Federal Reserve System to regulate the use of credit in securities transactions. The principal purpose of the various statutory provisions is to ensure the maintenance of fair and honest markets in securities transactions on the organized exchanges and in the over-the-counter markets.

REGULATION OF EXCHANGES AND EXCHANGE TRADING

Registration and Exemption of Exchanges

As of June 30, 1966, 14 stock exchanges were registered under the Exchange Act as national securities exchanges:

American Stock Exchange
Boston Stock Exchange
Chicago Board of Trade
Cincinnati Stock Exchange
Detroit Stock Exchange
Midwest Stock Exchange
National Stock Exchange
New York Stock Exchange
Pacific Coast Stock Exchange
Philadelphia-Baltimore-Washington Stock Exchange
Pittsburgh Stock Exchange
Salt Lake Stock Exchange
San Francisco Mining Exchange
Spokane Stock Exchange

Three exchanges have been exempted from registration by the Commission pursuant to Section 5 of the Act:

Colorado Springs Stock Exchange
Richmond Stock Exchange
Honolulu Stock Exchange

Review of Exchange Rules and Procedures

Rule 17a-8 of the Exchange Act provides that each national securities exchange must file with the Commission three copies of any proposed change in its rules not less than 3 weeks (or such shorter period as the Commission may authorize) before final action is taken by the exchange. These proposals are submitted for review to the Commission's Division of Trading and Markets. That Division also reviews, on a continuing basis, the existing rules, regulations, procedures, forms and practices of the national securities exchanges. The purposes of this review are to permit the Division to (a) ascertain the effectiveness of the application and enforcement by the exchanges of their own rules; (b) determine the adequacy of the rules of the exchanges, and of related statutory provisions and rules administered by the Commission, in light of changing market conditions, and (c) anticipate and define problem areas so that preventive or remedial steps can be taken. Most significant aspects of the rules and procedures of the national securities exchanges are subject to review by the staff in the course of a year.

When problems occur, conferences are held to permit the exchange and the Division to reach satisfactory solutions. These conferences sometimes lead to studies of current rules and practices, or proposed exchange's performance, the staff communicated its views to the particular exchange and discussions were held between the staff of the Commission and the exchange to arrive at appropriate solutions.

Commission Inspections of the Exchanges

Pursuant to the regulatory scheme of the Act, the Commission actively oversees the performance by the national securities exchanges of their self-regulatory activities. As part of this program, the Office of Regulation in the Division of Trading and Markets conducts regular inspections of various phases of exchange activity. During the past year, it conducted two such inspections of the New York Stock Exchange and three inspections of the American Stock Exchange. These inspections covered such areas as specialist and registered trader surveillance, exchange procedures for investigation and inquiry into unusual market situations, and exchange inspections of member firms' office procedures. In addition, the Office of Regulation carried out general inspections of the Philadelphia-Baltimore-Washington, Boston and Pittsburgh Stock Exchanges. The inspection program enables the Commission to insure that the exchanges are complying with their self-regulatory responsibilities and to recommend improvements and refinements designed to increase the effectiveness of self-regulation. Where it appeared to the Commission's staff that revisions in internal procedures or policies were desirable in order to improve an exchange's performance, the staff communicated its views to the particular exchange and discussions were held between the staff of the Commission and the exchange to arrive at appropriate solutions.

Proceedings Against San Francisco Mining Exchange

During the fiscal year, the Commission issued a decision pursuant to Section 19 (a) (1) of the Exchange Act in which it held that it was necessary and appropriate for the protection of investors to withdraw the registration of the San Francisco Mining Exchange as a national securities exchange.

The Commission found that over a period of years the Exchange had repeatedly neglected to enforce compliance by its members and by issuers of securities listed thereon with the reporting, insider trading and anti-fraud provisions of the Exchange Act and had lent its facilities to securities distributions made in violation of the registration requirements of the Securities Act of 1933. The Commission also found that officials of the Exchange had been personally involved in repeated violations of the securities acts. In rejecting the Exchange's request that it be given an opportunity to rehabilitate itself, the Commission pointed out that the Exchange had failed to avail itself of prior opportunities to take corrective measures, that it did not perform any significant function as a trading market, and that an effective rehabilitation would in effect require the organization of an entirely new exchange. On June 20, 1966, the Exchange filed a petition for review of the Commission's order with the Court of Appeals for the Ninth Circuit. The Court has issued a stay of the Commission's order pending final determination of the Exchange's petition.

Exchange Disciplinary Action

Each national securities exchange reports to the Commission disciplinary actions taken against its members, member firms, and their associated persons for violation of any rule of the exchange or of the Securities Exchange Act or any rule or regulation thereunder. During the fiscal year, eight exchanges reported 133 such actions, including impositions of fines in 44 cases ranging from $25 to $10,000, with total fines aggregating $68,575, and the suspension from membership of 14 individuals and 9 member organizations. These exchanges also reported the imposition of various sanctions against 65 registered representatives and employees of member firms. In addition, a number of informal staff actions of a cautionary nature were reported by several exchanges.

REGISTRATION OF SECURITIES ON EXCHANGES

Unless a security is registered on a national securities exchange under the Securities Exchange Act or is exempt from such registration it is unlawful for a member of such exchange or any broker or dealer to effect any transaction in the security on the exchange. In general, the Act exempts from registration obligations issued or guaranteed by a state or the Federal Government or by certain subdivisions or agencies thereof and authorizes the Commission to adopt rules and regulations exempting such other securities as the Commission may find necessary or appropriate to exempt in the public interest or for the protection of investors. Under this authority the Commission has exempted securities of certain banks, certain securities secured by property or leasehold interests, certain

warrants and, on a temporary basis, certain securities issued in substitution for or in addition to listed securities.

Pursuant to Section 12 of the Exchange Act, an issuer may register a class of securities on an exchange by filing with the Commission and the exchange an application which discloses pertinent information concerning the issuer and its affairs. Information must be furnished regarding the issuer's business, its capital structure, the terms of its securities, the persons who manage or control its affairs, the remuneration paid to its officers and directors, and the allotment of options, bonuses and profit-sharing plans, and financial statements certified by independent accountants must be filed as part of the application.

Form 10 is the form used for registration by most commercial and industrial companies. There are specialized forms for certain types of securities, such as voting trust certificates, certificates of deposit and securities of foreign governments.

STATISTICS RELATING TO SECURITIES ON EXCHANGES

Number of Issuers and Securities

As of June 30, 1966, a total of 2,578 issuers had 4,220 classes of securities listed and registered on national securities exchanges, of which 2,958 were classified as stocks and 1,262 as bonds. Of these totals 1,445 issuers had 1,648 stock issues and 1,161 bond issues listed and registered on the New York Stock Exchange. Thus, 56.1 percent of the issuers, 55.7 percent of the stock issues and 92 percent of the bond issues were on the New York Stock Exchange.

During the 1966 fiscal year, 161 issuers listed and registered securities on a national securities exchange for the first time, while the registration of all securities of 105 issuers was terminated. A total of 326 applications for registration of securities on exchanges was filed during the year.

Market Value of Securities Available for Trading

The market value on December 31, 1965, of stocks and bonds, both listed and unlisted, admitted to trading on one or more stock exchanges in the United States was approximately $707 billion.

There is no duplication of issues between the New York and American Stock Exchanges. The figures for all other exchanges are for the net number of issues appearing only on such exchanges, excluding the many issues on them which were also traded on one or the other of the New York exchanges. The number and market value of issues as shown below exclude those suspended from trading and a few others for which quotations were not available.

[table omitted]

The 3,067 preferred and common stock issues represented over 12.2 billion shares, of which 11.7 billion were included in the 2,900 issues listed on registered exchanges.

The New York Stock Exchange has reported aggregate market values of all stocks listed thereon monthly since December 31, 1924, when the figure was $27.1 billion. The American Stock Exchange has reported totals as of December 31 annually since 1936. Aggregates for stocks exclusively on the remaining exchanges have been compiled as of December 31 annually by the Commission since 1948. The available data since 1936 appear in Table 5 in the appendix of this Annual Report. It should be noted that changes in aggregate market values over the years reflect not only changes in prices of stocks but also such factors as new listings, mergers into listed companies, removals from listing and issuance of additional shares of a listed security.

Share and Dollar Volume of Stocks Traded

The figures below show the annual volume of shares traded on all exchanges during the years 1955 through 1965, and the first 6 months of 1966. These volume figures include stocks, warrants and rights. Tables 6 and 7 in the appendix of this Annual Report contain comprehensive statistics on volume, by exchanges.

[table omitted]

In 1965 share and dollar volume on exchanges increased 25.6 percent and 23.6 percent, respectively, over 1964. Volume continued to increase in the first 6 months of 1966. On the American Stock Exchange the dollar volume in these 6 months exceeded the dollar volume for the entire year 1965.

Foreign Stocks on Exchanges

The market value on December 31, 1965, of all shares and certificates representing foreign stocks on U.S. stock exchanges was $18.8 billion, of which $15.3 billion represented Canadian and $3.5 billion represented other foreign stocks. The market values of the entire Canadian stock issues were included in these aggregates. Most of the other foreign stocks were represented by American Depository Receipts or American shares, only the outstanding amounts of which were used in determining market values.

[table omitted]

The number of foreign stocks on the exchanges has declined in recent years, from 173 as of the end of 1960 to 130 in 1965. During this period, the American Stock Exchange had

a net decline from 145 to 99 issues, while the New York Stock Exchange had an increase of 1 and the remaining exchanges an increase of 2.

Trading in foreign stocks on the American Stock Exchange has fallen from 17.9 percent of the reported share volume in 1960 to 15.1 percent in 1965. On the New York Stock Exchange trading in foreign stocks has declined from 2.7 percent of its reported share volume in 1960 to 2 percent in 1965.

Comparative Exchange Statistics

During fiscal year 1966, there was a moderate increase in the number of stocks listed on the New York Stock Exchange, consistent with the trend of recent years. The number listed on the American Stock Exchange increased slightly, representing the second consecutive year in which a gain occurred. The number of stocks available for trading exclusively on the other exchanges continued to decline.

[table omitted]

In 1965, the aggregate value of shares listed on the New York Stock Exchange represented an increasing proportion of total share values on all exchanges as it has in most years since the late 1940's.

[table omitted]

The ratio of share volume on the regional exchanges to the total on all exchanges has continued to decline over the years. However, in 1965 the regional exchange percentage of dollar volume increased slightly. The American Stock Exchange percentages of share and dollar volume have increased steadily since 1963 while the percentages of the New York Stock Exchange have decreased. In the following presentation stocks, warrants and rights are included. Annual data since 1935 are shown in Appendix Table 7 in this Annual Report.

[table omitted]

DELISTING OF SECURITIES FROM EXCHANGES

Application may be made to the Commission by exchanges to strike securities or by issuers to withdraw their securities from listing and registration on exchanges pursuant to Rule 12d2-2 under Section 12 (d) of the Securities Exchange Act. During the fiscal year ended June 30, 1966, the Commission granted applications by exchanges and issuers to remove 63 stock issues and 2 bond issues, representing 60 issuers, from listing and registration. Since 5 stocks were each delisted by two exchanges, there was a total of 68 stock removals, as follows:

[table omitted]

The three applications by issuers which were granted during the year removed one security each from the American, Pacific Coast and Philadelphia-Baltimore-Washington Stock Exchanges.

UNLISTED TRADING PRIVILEGES ON EXCHANGES

Stocks with unlisted trading privileges which are not also listed and registered on other exchanges continued to decline in number, from 132 on June 30, 1965, to 114 on June 30, 1966. The American Stock Exchange accounted for the entire decline except for 1 issue removed from the Philadelphia-Baltimore-Washington Stock Exchange. During the calendar year 1965, the reported volume of trading on the exchanges in stocks with only unlisted trading privileges similarly declined to about 23,775,000 shares, or about .92 percent of the total share volume on all exchanges, from about 24,521,000 shares and about 1.2 percent of share volume during calendar year 1964.

About 97 percent of the 1965 volume was on the American Stock Exchange while four other exchanges contributed the remaining 3 percent. The share volume in these stocks on the American Stock Exchange represented 4 percent of the total share volume on that exchange.

Unlisted trading privileges on exchanges in stocks listed and registered on other exchanges numbered 1,735 as of June 30, 1966. The volume of trading in these stocks for the calendar year 1965 was reported at about 87,761,000 shares. About 17.4 percent of this volume was on the American Stock Exchange in stocks listed on regional exchanges and 82.6 percent was on regional exchanges in stocks listed on the New York or American Stock Exchange. While the 87,761,000 shares amounted to only 3.4 percent of the total share volume on all exchanges, they constituted substantial portions of the share volume of most regional exchanges, as reflected in the following approximate percentages: Cincinnati, 84 percent; Boston, 78 percent; Detroit, 75 percent; Philadelphia-Baltimore-Washington, 71 percent; Pittsburgh, 50 percent; Midwest, 31 percent; and Pacific Coast, 30 percent.

Applications for Unlisted Trading Privileges

Applications by exchanges for unlisted trading privileges in stocks listed on other exchanges, filed pursuant to Rule 12f-1 under Section 12 (f) (1) (B) of the Securities Exchange Act, were granted by the Commission during the fiscal year ended June 30, 1966, as follows:

[table omitted]

BLOCK DISTRIBUTIONS REPORTED BY EXCHANGES

The usual method of distributing blocks of listed securities considered too large for the auction market on the floor of an exchange is to resort to "secondary distributions" over the counter after the close of exchange trading. Secondary distributions, as reported since 1942, reached a new high of $1,603,107,000 during the calendar year 1965, surpassing the previous peak of $926,514,000 in 1961. During the first 6 months of 1966, there were 72 secondary distributions aggregating $1,126,091,000. Unusually large secondary distributions have caused these record high figures. Secondary distributions of the common stocks of Ford Motor Co. and General Motors Corp. accounted for 38 percent of the 1965 total value, and a distribution of Trans World Airlines common stock comprised more than half the .total for the first 6 months of 1966.

[table omitted]

Special Offering Plans were adopted by many of the exchanges in 1942, and Exchange Distribution Plans in 1953, in an effort to keep as much trading as possible on their floors. Since 1962 there have been no special offerings. Exchange distributions increased to reach a record of 72 in 1963 but have since declined. In 1965 there were 57 with a value of $86,479,000.

OVER-THE-COUNTER TRADING IN COMMON STOCKS TRADED ON NATIONAL SECURITIES EXCHANGES

Pursuant to the recommendations of the Special Study of Securities Markets, the Commission in December 1964 adopted Rule 17a-9 providing a system for the identification of broker-dealers making off-board markets in common stocks traded on national securities exchanges and for the reporting of summaries of over-the-counter trading in common stocks traded on national securities exchanges (sometimes referred to as the "third market").

In accordance with this rule, since January 1965 brokers and dealers who make markets in common stocks traded on national securities exchanges have been reporting their trading over the counter and on exchanges in the common stocks in which they make markets. They also report certain off-board trading in other common stocks traded on exchanges. Broker-dealers who are not market makers report certain large third market transactions. The reporting system is designed to reflect all sales to persons other than broker-dealers, i.e., to individuals and institutions.

During the calendar year 1965, total third market sales of common stock amounted to 50,362,000 shares valued at $2,563,000,000. This latter figure was the equivalent of 2.9

percent of the value of shares of common and preferred stocks traded on all national securities exchanges. Almost 98 percent of the third market dollar volume was in common stocks listed on the New York Stock Exchange. Over-the-counter sales of these stocks during 1965 amounted to the equivalent of 3.4 percent of the New York Stock Exchange's value of trading in common and preferred issues.

In the first half of 1966, third market volume was larger than in the corresponding period of 1965 but did not keep pace with the sharply increased volume on exchanges. In this period, third market sales of common stocks amounted to 31,009,000 shares valued at $1,596,000,000, or 2.3 percent of the dollar volume on all national securities exchanges.

MANIPULATION AND STABILIZATION

Manipulation; Market Surveillance

The Exchange Act and Commission rules under the Act prohibit various kinds of manipulative activities. In order to enable the Commission to meet its responsibilities for the surveillance of the securities markets, the market surveillance staff has devised a number of procedures to identify possible manipulative activities. A program has been adopted with respect to surveillance over listed securities, in which the staff's activities are closely coordinated with the stock watching operations of the New York and American Stock Exchanges. Within this framework, the staff reviews the daily and periodic stock watch reports prepared by these exchanges and on the basis of its analysis of the information developed by the exchanges and other sources, determines matters of interest, possible violations of applicable law, and the appropriate action to be taken.

In addition, the market surveillance staff maintains a continuous ticker tape watch of transactions on the New York and American Stock Exchanges and the sales and quotations sheets of regional exchanges to observe any unusual or unexplained price variations or market activity. The financial news ticker, leading newspapers and various financial publications and statistical services are also closely followed. Matters raised by private investors in letters to the Commission may also be used in determining whether possible violations have occurred.

If any of these sources reveal possible violations, the market surveillance staff conducts a preliminary inquiry into the matter. These inquiries, some of which are conducted with the cooperation of the exchange concerned, generally begin with the identification of the brokerage firms which were active in the security. Contact may be made with partners, officers or registered representatives of the firms, with customers, or with officials of the company in question to determine the reasons for the activity or price change in the securities involved and whether violations may have occurred.

The Commission, recognizing the utility of electronic data-processing equipment, has developed an automated over-the-counter surveillance program to provide more efficient and comprehensive surveillance. The automated equipment is programmed to identify, among other things, unlisted securities whose price movement or dealer interest varies beyond specified limits in a pre-established time period. When a security is so identified, the automated system prints out current and historic market information concerning it. This data, combined with other available information, is collated and analyzed to select those securities whose activity indicates the need for further inquiry or referral to the Commission's enforcement staff.

Stabilization

Stabilization involves open-market purchases of securities to prevent or retard a decline in the market price in order to facilitate a distribution. It is permitted by the Exchange Act subject to the restrictions provided by the Commission's Rules 10b-6, 7, and 8. These rules are designed to confine stabilizing activity to that necessary for the above purpose, to require proper disclosure and to prevent unlawful manipulation.

During fiscal year 1966, stabilizing was effected in connection with stock offerings totaling 57,793,000 shares having an aggregate public offering price of $2,158,883,000 and bond offerings having a total offering price of $247,974,000. In these offerings, stabilizing transactions resulted in the purchase of 1,992,000 shares at a cost of $85,974,000 and bonds at a cost of $2,078,000. In connection with these stabilizing transactions, 9,761 stabilizing reports, showing purchases and sales of securities effected by persons conducting the distribution, were received and examined during the fiscal year.

REGISTRATION OF OVER-THE-COUNTER SECURITIES

As previously noted, Section 12 (g) of the Exchange Act requires the registration of securities traded over the counter, when certain standards as to assets of the issuer and number of shareholders are met. The same forms used for the registration of securities on an exchange are used for the registration of over-the-counter securities. Part II of this report includes statistics regarding the number of registration statements filed during the fiscal year pursuant to Section 12 (g) and related matters.

PERIODIC REPORTS

Section 13 of the Exchange Act requires issuers of securities registered pursuant to Section 12 to file periodic reports keeping current the information contained in the application for registration or registration statement. These periodic reports include annual, semi-annual, and current reports. The principal annual report form is Form 10-K,

which is designed to give current information regarding the matters covered in the original filing. Semi-annual reports required to be filed on Form 9-K are devoted chiefly to furnishing mid-year financial data. Current reports on Form 8-K are required to be filed for each month in which any of certain specified events of immediate interest to investors have occurred. A report on this form deals with matters such as changes in control of the registrant, important acquisitions or dispositions of assets, the institution or termination of important legal proceedings and important changes in the issuer's capital securities or in the amount thereof outstanding. Section 15 (d) of the Exchange Act, generally speaking, requires issuers who have filed registration statements under the Securities Act of 1933 that have become effective to file the same reports as the issuers described above.

The following table shows the number of reports filed during the fiscal year pursuant to Sections 13 and 15 (d) of the Exchange Act. As of June 30, 1966, there were 2,578 issuers having securities listed on a national securities exchange and registered under Section 12 (b) of the Act, 2,061 issuers having securities registered under Section 12 (g), and 2,233 additional issuers (including 358 that were also registered as investment companies under the Investment Company Act of 1940) which were subject to the reporting requirements of Section 15 (d) of the Act.

[table omitted]

REGULATION OF PROXIES

Scope of Proxy Regulation

Regulation 14A, adopted pursuant to Sections 14 (a) of the Securities Exchange Act, 12 (e) of the Public Utility Holding Company Act of 1935, and 20 (a) of the Investment Company Act of 1940, requires the disclosure in a proxy statement of pertinent information in connection with the solicitation of proxies, consents and authorizations in respect of securities subject to those provisions, in order to enable holders of such securities to act intelligently on the matters involved. The regulation also provides, among other things, that when the management is soliciting proxies, any security holder desiring to communicate with other security holders for a proper purpose may require the management to furnish him with a list of all security holders or to mail his communication to security holders for him. A security holder may also, subject to reasonable prescribed limitations, require the management to include in its proxy material any appropriate proposal which such security holder desires to submit to a vote of security holders. Any security holder or group of security holders may at any time make an independent proxy solicitation upon compliance with the proxy rules, whether or not the management is making a solicitation. Certain additional provisions of the regulation are applicable where a contest for control of the management of an issuer or representation on the board is involved.

Copies of proposed proxy material must be filed with the Commission in preliminary form prior to the date of the proposed solicitation. Where preliminary material fails to meet the prescribed disclosure standards, the management or other group responsible for its preparation is notified informally and given an opportunity to correct the deficiencies in the preparation of the definitive proxy material to be furnished to security holders.

The Securities Acts Amendments of 1964 extended the proxy solicitation requirements to those over-the-counter securities which are registered under Section 12 (g) of the Act. In addition, new Section 14 (c) of the Act provides that issuers of securities registered under Section 12 shall, in accordance with rules and regulations prescribed by the Commission, transmit information comparable to proxy material to security holders from whom proxies are not solicited. During the fiscal year the Commission adopted Regulation 14C implementing this statutory provision.

Statistics Relating to Proxy and Stockholder Information Statements

During the 1966 fiscal year, 4,109 proxy statements in definitive form were filed under the Commission's Regulation 14A for the solicitation of proxies of security holders; 4,084 of these were filed by management and 25 by non-management groups or individual stockholders. These 4,109 solicitations related to 3,773 companies, some 336 of which had 2 solicitations during the year, the second generally for a special meeting not involving the election of directors.

There were 3,632 solicitations of proxies for the election of directors, 446 for special meetings not involving the election of directors, and 31 for assents and authorizations.

During fiscal year 1966, the votes of security holders were solicited with respect to the following types of matters, other than the election of directors:

[table omitted]

During fiscal year 1966, 53 information statements under new Regulation 140 were filed by 52 companies, 1 company filing 2 such statements. The 53 statements related to 48 annual meetings and 5 special meetings.

Stockholders' Proposals

During the 1966 fiscal year, 156 proposals submitted by 35 stockholders were included in the proxy statements of 103 companies under Rule 14a-8 of Regulation 14A.

Typical of such stockholder proposals submitted to a vote of security holders were resolutions relating to amendments of charters or bylaws to provide for cumulative voting for the election of directors, limitations on the grant of stock options to, and their exercise

by, key employees and management groups, the sending of a post-meeting report to all stockholders, and a change of the place of the annual stockholders' meeting.

A total of 58 additional proposals submitted by 39 stockholders was omitted from the proxy statements of 30 companies in accordance with Rule 14a-8. The principal reasons for such omissions and the number of times each such reason was involved (counting only one reason for omission for each proposal even though it may have been omitted under more than one provision of Rule 14a-8) were as follows:

[table omitted]

Ratio of Soliciting to Non-Soliciting Companies

Of the 2,578 issuers that had securities listed and registered on national securities exchanges as of June 30, 1966, 2,357 had voting securities so listed and registered. Of these 2,357 issuers, one listed and registered voting securities for the first time after its annual stockholders' meeting in fiscal 1966; of the remaining 2,356 issuers with voting securities, 2,141 or 90.9 percent, solicited proxies under the Commission's proxy rules during the 1966 fiscal year for the election of directors.

Proxy Contests

During the 1966 fiscal year, 37 companies were involved in proxy contests for the election of directors. A total of 923 persons, both management and non-management, filed detailed statements as participants under the requirements of Rule 14a-11. Proxy statements in 24 cases involved contests for control of the board of directors and those in 13 cases involved contests for representation on the board.

Management retained control in 10 of the 24 contests for control of the board of directors, 2 were settled by negotiation, non-management persons won 6 and 6 were pending as of June 30, 1966. Of the 13 cases where representation on the board of directors was involved, management retained all places on the board in 6 contests, opposition candidates won places on the board in 6 cases and 1 was settled by negotiation.

INSIDERS' SECURITY HOLDINGS AND TRANSACTIONS

Corporate insiders, by virtue of their position, may have knowledge of a company's condition and prospects which is unavailable to the general public and may be able to use such information to their personal advantage in trading in the company's securities. Section 16 of the Securities Exchange Act and corresponding provisions in Sections 17 of the Public Utility Holding Company Act of 1935 and Section 30 (f) of the Investment Company Act of 1940 are designed to provide other stockholders and investors with information as to insiders' security transactions and holdings, and to prevent the unfair

use of confidential information by insiders to profit from short-term trading in a company's securities.

Ownership Reports

Section 16 (a) of the Securities Exchange Act, as amended, requires every person who beneficially owns, directly or indirectly, more than 10 percent of any class of equity security which is registered under Section 12 (b) for exchange listing or under Section 12 (g) for over-the-counter trading, or who is a director or an officer of the issuer of any such security, to file statements with the Commission disclosing his ownership of the issuer's equity securities and changes in ownership. Copies of such statements must also be filed with exchanges on which securities are listed. Similar provisions applicable to insiders of registered public-utility holding companies and registered closed-end investment companies are contained in Section 17 (a) of the Public Utility Holding Company Act and Section 30 (f) of the Investment Company Act. The administration of the insider reporting provisions of the three Acts is combined in one section in the Division of Corporation Finance.

During the fiscal year, 96,232 ownership reports (23,989 initial statements of ownership on Form 3 and 72,243 statements of changes in ownership on Form 4) were filed with the Commission. This represents an increase of 51,601 over the 44,631 reports filed during the 1964 fiscal year and an increase of 39,678 over the 56,554 reports filed during the 1965 fiscal year. The bulk of the increase is attributable to the extension of the reporting requirements to insiders of issuers of over-the-counter securities registered under Section 12 (g).

All ownership reports are made available for public inspection as soon as they are filed at the Commission's office in Washington and at the exchanges where copies are filed. In addition, the information contained in reports filed with the Commission is summarized and published in the monthly "Official Summary of Security Transactions and Holdings," which is distributed by the Government Printing Office on a subscription basis to more than 25,000 persons.

Recovery of Short-Swing Trading Profits by Issuer

In order to prevent insiders from making unfair use of information which they may have obtained by reason of their relationship with a company, Section 16 (b) of the Exchange Act, Section 17 (b) of the Holding Company Act, and Section 30 (f) of the Investment Company Act provide for the recovery by or on behalf of the issuer of any profit realized by insiders (in the categories listed above) from certain purchases and sales, or sales and purchases, of securities of the company within any period of less than 6 months. The Commission has certain exemptive powers with respect to transactions not comprehended within the purpose of these provisions, but is not charged with the enforcement of the civil remedies created by them.

INVESTIGATIONS WITH RESPECT TO REPORTING PROVISIONS

Section 21 (a) of the Act authorizes the Commission to make such investigations as it deems necessary to determine whether any person has violated or is about to violate any provision of the Act or any rule or regulation thereunder. The Commission is authorized, for this purpose, to administer oaths, subpoena witnesses, compel their attendance, take evidence and require the production of records. In addition to the investigations undertaken in enforcing the anti-fraud, broker-dealer registration, and other regulatory provisions of the Act, which are discussed in Part XI of this report under "Complaints and Investigations," the following investigations were undertaken in connection with the enforcement of the reporting provisions of Sections 12, 13, 14 and 15 (d) of the Act and the rules thereunder, particularly those provisions relating to the filing of annual and other periodic reports and proxy material:

[table omitted]

REGULATION OF BROKER-DEALERS AND OVER-THE-COUNTER MARKETS

Registration

Subject to limited exemptions, Section 15 (a) of the Securities Exchange Act requires the registration of all brokers and dealers who use the mails or instrumentalities of interstate commerce to effect or induce transactions in securities in the over-the-counter market, Brokers and dealers conducting an exclusively intrastate business or dealing only in exempted securities, commercial paper, commercial bills or bankers' acceptances are exempt from registration.

The following tabulation reflects certain data with respect to registrations of brokers and dealers during the fiscal year ended June 30, 1966.

[table omitted]

Administrative Proceedings

The scope of the administrative sanctions which the Commission may impose against brokers and dealers and persons associated with a broker or dealer, pursuant to Sections 15 (b) and 15A of the Exchange Act, was enlarged in significant respects by the Securities Acts Amendments of 1964. Thus, in addition to the previously available sanctions against a broker-dealer of denial or revocation of registration and expulsion or suspension from a registered securities association or national securities exchange, the

Commission may now suspend a broker-dealer's registration for a period not to exceed 12 months and may impose censure. Under prior law the Commission could not proceed directly against individuals associated with a broker-dealer firm, although incidental to a proceeding against the firm it could make findings with respect to such individuals which had the effect of disqualifying them from employment in the securities industry. The Act, as amended, permits direct action against associated persons, with or without joining the firm. The Commission may censure an associated person, may suspend or bar him from being associated with a broker or dealer, and may suspend or bar him from being associated with a member of a registered securities association.

Under Section 15 (b), a sanction of revocation, denial or suspension of registration, or censure may be imposed upon a broker-dealer if, after notice and opportunity for hearing, the Commission finds that such sanction is in the public interest and that the broker-dealer, or any person associated with such broker-dealer, is subject to one or more of the specified statutory disqualifications. The Commission may censure, or bar or suspend from association with a broker-dealer, an associated person where it finds that such action is in the public interest and that such person has committed or omitted any act or omission which would be a basis for the imposition of a sanction if such person were a broker-dealer. The statutory disqualifications, which have been enlarged by the 1964 amendments, include the following:

(1) wilfully false or misleading statements in an application for registration or other report required to be filed under the Exchange Act;

(2) conviction within the previous 10 years of a felony or misdemeanor which involved the purchase or sale of securities; arose out of the conduct of business as a broker-dealer or investment adviser; involved embezzlement, fraudulent conversion, or misappropriation of funds or securities; or involved violation of the provisions of the United States Code dealing with various frauds and swindles committed by use of the mails, telephone, telegraph, radio or television;

(3) injunction by a court of competent jurisdiction against engaging in certain practices related to the securities business;

(4) wilful violation of any provision of the Securities Act of 1933, the Exchange Act, the Investment Advisers Act of 1940 or the Investment Company Act of 1940 or any of the Commission's rules or regulations thereunder;

(5) wilfully aiding or abetting another person in a violation of the Federal securities laws or rules and regulations thereunder or failing reasonably to supervise other persons who commit such violations; and

(6) employing a person barred or suspended from being associated with a broker-dealer.

Section 15A of the Exchange Act as amended empowers the Commission to suspend or expel a broker-dealer from membership in a registered securities association or to suspend or bar any person from being associated with a member, upon a finding of violation of the Federal securities laws or any rule or regulation thereunder. The National Association of Securities Dealers, Inc. (NASD) is the only such association. Section 19 (a) (3) of the Act gives the Commission power to take similar action against members of national securities exchanges.

Set forth below are statistics with respect to administrative proceedings instituted by the Commission pursuant to Sections 15 (b), 15A and 19 (a) (3) of the Securities Exchange Act which were pending during fiscal year 1966.

[table omitted]

Decisions of Particular Interest

It is not feasible to discuss within the confines of this report each of the many decisions rendered by the Commission during the 1966 fiscal year in administrative proceedings with respect to broker-dealers and their personnel. However, a few cases of unusual interest or significance are summarized in the following paragraphs:

The Commission's decision in Shearson, Hammill& Co., involving one of the major Wall Street brokerage houses, was of particular interest to the financial community. The Commission found that certain activities which had taken place in three California branch offices of the firm, primarily in Los Angeles, resulted in violations of both the registration provisions of the Securities Act and the anti-fraud provisions of that Act, the Exchange Act, and the Investment Advisers Act. A significant aspect of the case is that the Commission held responsible not only the firm and certain branch office personnel directly involved in the misconduct, but also the firm's five principal partners who comprised its executive committee charged with supervision of the firm's nationwide operations. The Commission found that their failure "diligently to enforce (the firm's) system of internal controls resulted in the perpetration of fraud upon many customers," and that these principals bore "a heavy responsibility" for the violations.

The Commission stated that the willful violations established "were so grave and extensive as to warrant the imposition of substantial sanctions." However, the firm had terminated the employment of most of the branch office personnel involved in the violations and by the adoption of enlarged internal controls had reduced the risk of any recurrence of injury to investors of the type found, and the Commission recognized that further sanctions against the firm would affect many innocent people. In view of these factors, the Commission concluded that it would be inclined to withhold imposition of a sanction against the firm if the members of the executive committee were dissociated from the firm for an appropriate period. Accordingly, it withheld issuance of an order to permit the firm to submit a proposal providing for the separation of those persons from

the firm for 60 days each and for their surrender of any share in firm profits during that period. A proposal was thereafter submitted, and approved by the Commission, which provided that during the period of dissociation the executive committee members would not receive, directly or indirectly, any salary or share of the profits, and that all salaries and profits attributable to that period would be distributed as a stock dividend to the stockholders of the firm's successor corporation other than the executive committee members. A compliance report submitted in August 1966 disclosed that the profits allocable to the period of dissociation were $573,168, that salaries and consulting fees which would have been payable but were not paid to the executive committee members amounted to $24,790, and that the total of these amounts had been distributed in the form of a stock dividend.

The case of Russell L. Irish involved a broker-dealer specializing in the retail sale of mutual fund shares. The Commission found that Irish, contrary to the best interests of his customers and for his own gain, induced purchases and redemptions of such shares in the accounts of customers which were excessive in size and frequency in view of the "non-trading" character of those accounts. Among other things, he followed a policy of recommending to customers that they redeem the shares of one fund and use the proceeds to buy those of another fund, requiring the payment of a new sales commission. Many of these switches were effected within a relatively short time after shares in the first fund had been acquired. This policy, the Commission found, was highly profitable to Irish and detrimental to his customers. In addition, Irish sold mutual fund shares to customers in amounts slightly below the "break-point" at which a reduced sales load would have been available, without adequately disclosing the savings which could have been obtained through slightly larger investments. The Commission concluded that Irish's conduct violated the anti-fraud provisions of the securities acts and that it was appropriate in the public interest to revoke his registration.

In Lile & Co., Inc. the Commission found, among other things, that the firm's president and sole stockholder obtained loans from a customer of the firm, for the purpose of financing the firm, and in doing so made misrepresentations to the customer. The president represented that the firm's business was good and would be expanded and failed to disclose the firm's actual precarious financial condition. In finding that this conduct was fraudulent, the Commission stated that "The propriety of inducing a customer to make substantial loans for the purpose of financing an unprofitable broker-dealer would seem to be particularly questionable in any case where, as here, the broker-dealer had established a relationship of trust and confidence with the customer. At the least, where such loans are solicited, the anti-fraud provisions require candid disclosure to the customer of all the material facts."

A significant aspect of the decision in Clarence Earl Thornton was the holding that a state-licensed broker-dealer, who with knowledge of Thornton's purchase of securities from a customer at a price far below the market price loaned the purchase price to Thornton in anticipation of purchasing the securities from him at a discount, had aided

and abetted Thornton's fraudulent conduct. The Commission revoked Thornton's registration and found the other broker-dealer a cause of the revocation.

As in the past, a number of cases decided during the year involved so-called "boiler-rooms." Among these cases were Hamilton Waters & Co., Inc. and M. J. Merritt &, Co., Inc., in both of which the Commission found that the respondents had engaged in the sale of securities by means of high pressure selling techniques including the use of false and misleading statements concerning the securities being sold and their issuers. As is typical of "boiler-room" activities, the securities involved were unseasoned and speculative and were generally sold to persons with whom the respondents were not acquainted and in disregard of the financial needs and objectives of such persons. The Commission revoked the broker-dealer registrations of both firms and found various individuals associated with the firms, who either participated directly in the misconduct or by virtue of their position or interest in the firms were responsible for it, to be "causes" of the revocation.

Suspension of Registration Pending Final Determination

Section 15 (b) of the Securities Exchange Act authorizes the Commission to suspend a broker-dealer's registration pending final determination as to whether registration should be revoked. In order to suspend registration, the Commission must find, after notice and opportunity for hearing, that suspension is necessary or appropriate in the public interest or for the protection of investors. The registration of one broker-dealer was suspended during the past fiscal year on the basis of such findings. The entry of a suspension order is of course not determinative of the ultimate issue whether registration should be revoked.

Net Capital Rule

Rule 15c3-1 under the Exchange Act, commonly known as the net capital rule, was amended during fiscal year 1965 to impose minimum net capital requirements on brokers and dealers (effective December 1, 1965) and in certain other respects. As before, the rule limits the amount of indebtedness which may be incurred by a broker-dealer in relation to its capital, by providing that the "aggregate indebtedness" of a broker-dealer may not exceed 20 times the amount of its "net capital" as computed under the rule. During the past fiscal year, violations of the net capital rule were charged in eight administrative proceedings instituted against broker-dealers.

Registered broker-dealers who participate in "firm commitment" underwritings must have sufficient capital to permit the participation provided by the underwriting contract without impairing the capital-debt ratio or minimum net capital prescribed by the rule. If a broker-dealer is unable to meet such requirements, he must decrease his "firm commitment" to the extent necessary to achieve compliance with the rule. If necessary, he may have to withdraw from the underwriting or participate on a "best efforts" basis only.

Financial Statements

Rule 17a-5 under Section 17 (a) of the Exchange Act requires registered broker-dealers to file annual reports of financial condition with the Commission. Such reports must be certified by a certified public accountant or public accountant who is in fact independent, with certain limited exemptions applicable to situations where certification does not appear necessary for customer protection. A broker-dealer's first report must reflect his financial condition as of a date between the end of the 1st and 5th months after the effective date of registration. All reports must be filed within 45 days after the date as of which the report speaks.

Through these reports the Commission and the public may evaluate the financial position and responsibility of broker-dealers. The financial report is one means by which the staff of the Commission determines whether the registrant is in compliance with the net capital rule. Failure to file the required reports may result in the institution of administrative proceedings.

During the fiscal year 4,134 reports of financial condition were filed with the Commission, compared to the 1965 total of 4,317.

Broker-Dealer Inspections

Section 17 (a) of the Exchange Act provides for regular and periodic inspections of registered broker-dealers. During the fiscal year a total of 1,272 such inspections was conducted. Inspections provide one of the most useful means available to the Commission for the protection of investors. Among other things, the staff members conducting the inspection determine a broker-dealer's financial condition, review his pricing practices, evaluate the safeguards employed in handling customers' funds and securities, and determine whether adequate and accurate disclosures are made to customers.

The Commission's inspectors also determine whether brokers and dealers are maintaining books and records as required by the Exchange Act and the Commission's rules thereunder and are conforming to the margin and other requirements of Regulation T of the Board of Governors of the Federal Reserve System. Inspectors also look for excessive trading or switching in customers' accounts. They frequently find evidence of the sale of unregistered securities or of fraudulent practices such as use of improper sales literature or sales techniques.

When an inspection reveals that a broker-dealer is in violation of applicable statutory provisions or rules, the action taken depends on the type of violation and its effect on the public. The Commission does not take formal action as a result of every infraction discovered. However, if the violation appears to be wilful and the public interest is best

served by formal action against the broker-dealer, the Commission promptly institutes appropriate proceedings.

The table below shows the types of infractions uncovered by the inspection program during the fiscal year:

[table omitted]

SUPERVISION OF ACTIVITIES OF NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

Section 15A of the Exchange Act provides for registration with the Commission of national securities associations and establishes standards and requirements for such associations. The National Association of Securities Dealers, Inc. (NASD) is the only association registered under the Act. The Act contemplates that such associations will serve as a medium for self-regulation by over-the-counter brokers and dealers. Their rules must be designed to protect investors and the public interest, to promote just and equitable principles of trade, and to meet other statutory requirements. They are to operate under the general supervision of the Commission, which is authorized to review disciplinary actions taken by them and to consider all changes in their rules. Review of the NASD rules, generally speaking, is carried out in the same manner and for similar purposes as the review of exchange rules described above.

In adopting legislation permitting the formation and registration of national securities associations, Congress provided an incentive to membership by permitting such associations to adopt rules which preclude a member from dealing with a non-member except on the same terms and conditions as the member affords the investing public. The NASD has adopted such rules. Accordingly, membership is necessary to profitable participation in underwritings since members may properly grant price concessions, discounts and similar allowances only to other members. Loss or denial of membership due to expulsion or suspension or other ineligibility due to a statutory disqualification, or the failure to meet standards of qualification established in NASD rules, may thus constitute a severe economic sanction.

At the close of the fiscal year the NASD had 3,707 members, reflecting a net decrease of 158 members during the year. This decrease was the net result of 229 admissions to and 387 terminations of membership. At the end of the year NASD member firms had 5,025 branch offices, reflecting a net increase of 197 offices during the year. This increase was the net result of the opening of 768 new offices and the closing of 571 offices. During the year the registered representative population, which generally includes all partners, officers, traders, salesmen and other persons employed by or affiliated with member firms in capacities which involve their doing business directly with the public, increased by 6,798 to stand at 83,641 as of June 30, 1966. This increase was the net result of

13,424: initial registrations, 11,418 re-registrations and 18,044 terminations of registrations during the year.

NASD Disciplinary Actions

The Commission receives from the NASD copies of its decisions in all disciplinary actions against members and registered representatives. In general, such actions are based on allegations that the respondents violated specified provisions of the NASD's Rules of Fair Practice. Where violations are found the NASD may impose one or more sanctions upon a member, including expulsion, suspension, fine, or censure. If the violator is an individual, his registration as a representative may be suspended or revoked, he may be suspended or barred from being associated with all members, and he may be fined and/or censured. Under Section 15A (b) (4) of the Exchange Act and the NASD's bylaws, no broker-dealer may be admitted to or continued in NASD membership without Commission approval if he has been suspended or expelled from membership in the NASD or a national securities exchange; he is barred or suspended from association with a broker or dealer or with all members of the NASD or an exchange; his registration as a broker-dealer has been denied, suspended, or revoked; he has been found to be a cause of certain sanctions imposed upon a member by the Commission, the NASD or an exchange; or he has associated with him any person subject to one of the above disqualifications.

During the past fiscal year the Association reported to the Commission its final disposition of disciplinary complaint actions against 197 member firms and 167 individuals associated with them. With respect to 52 members, complaints were dismissed as a result of findings that the allegations of violations had not been sustained. [Footnote: The majority of the cases where allegations against members were dismissed involved misuse of customers' and/or firm securities or funds by a representative under such circumstances that the member could not have known of or prevented the impropriety. The Securities Acts Amendments of 1964 authorized registered securities associations to take disciplinary action directly against individuals associated with members. The NASD has amended its rules to provide for such action. In the fiscal year there were eight cases in which the sole respondents were individuals associated with members.] In the remaining cases, violations were found and penalties were imposed on 145 members and 115 registered representatives or other individuals. The maximum penalty of expulsion from membership was imposed against 14 members, and 6 members were suspended from membership for periods ranging from 15 days to 3 months. In many of these cases, substantial fines were also imposed. In another 104 cases, members were fined amounts ranging from $50 to $7,500. In 21 cases, the only sanction imposed was censure, although censure was usually a secondary penalty where a more severe penalty was also imposed.

Various penalties were also imposed on registered representatives found in violation of NASD rules. The registrations of 50 representatives were revoked, and 23 representatives

had their registration suspended for periods ranging from 30 days to 18 months. [Footnote: As has been noted, a person found a cause of the expulsion or suspension of a member is disqualified from association with a member. The cause finding is therefore often used where an individual found to have violated Association rules should have been but was not registered as a registered representative. The numbers used in the text combine unregistered individuals found to have been a cause of the expulsion or suspension of a member with registered representatives whose registrations were revoked or suspended, since this is the practical consequence of a cause finding.] Fines in various amounts were also imposed against many revoked or suspended representatives. In addition, 42 other representatives were censured and/or fined amounts ranging from $100 to $10,000. Complaints against 52 representatives were dismissed on findings that no violations had been established.

Commission Review of NASD Disciplinary Action

Section 15A (g) of the Act, as amended, provides that disciplinary actions by the NASD are subject to review by the Commission on its own motion or on the timely application of any aggrieved person. This Section also provides that upon application for or institution of review by the Commission the effectiveness of any penalty imposed by the NASD is automatically stayed pending Commission review, unless the Commission otherwise orders after notice and opportunity for hearing. Section 15A (h) of the Act defines the scope of the Commission's review. If the Commission finds that the disciplined party committed the acts found by the NASD and thereby violated the rules specified in the determination, and that such conduct was inconsistent with just and equitable principles of trade, the Commission must sustain the NASD's action unless it finds that the penalties imposed are excessive or oppressive, in which case it must cancel or reduce them.

At the start of the fiscal year, 19 NASD disciplinary decisions were pending before the Commission on review. During the year 13 additional cases were brought up for review. Seventeen cases were disposed of by the Commission. In 14 of these cases, the Commission sustained the disciplinary action taken by the NASD, in one it set aside the Association action, and in the remaining two cases the Commission reduced the penalties imposed by the Association. Fifteen cases were pending as of the end of the year.

In the course of the year there were two important decisions concerning the obligation of members to exercise adequate supervision over employees.

The Commission sustained the NASD's action expelling L. B. Securities Corporation from membership in the Association and revoking the registration as a registered representative of R. B. Marx, its president and sole stockholder. The action of the NASD was in large part based upon the activities of C. Mackie Brown, Jr., a salesman, who was found to have violated the Association's fraud rule by causing the firm to send

confirmations for the purchase of stock of L. F. Popell & Co., Inc. ("Popell") to two customers who had never ordered the stock.

According to the Commission's opinion, at a time when L. B. Securities was making a market in Popell stock, Marx had telephone conversations with Brown who was then employed by another member and, being impressed by his selling abilities, offered him a position. Marx had never met Brown and knew nothing about his character and background. Marx's pre-employment investigation consisted of a telephone conversation with Brown's former employer who told Marx that he had had some "problems" with Brown, but that if he "could be controlled he would be a heck of a salesman." The nature of the problems was not identified and Marx did not inquire about them. While Marx claimed that he had received a favorable recommendation concerning Brown from other firms who were trading Popell stock, the Commission noted that Brown had never been employed by-any of these firms and that it appeared that the recommendations were related to his selling abilities.

The Commission found that during the 2 weeks Brown was employed by L. B. Securities he sold large quantities of Popell stock to his prior customers and that he was given a free hand and no attempt was made to supervise him. The Commission rejected applicants' excuse that they were unable to supervise Brown because Marx was the firm's sole supervisor and the market for Popell stock during Brown's association with the firm was hectic and disorderly. It stated that it was incumbent upon applicants to provide supervisory controls adequate to the business being conducted and added that this duty was "heightened by the fact that they were permitting a newly hired salesman with a doubtful recommendation to engage in selling activities, directed to customers who were not known to the applicants, in a highly speculative security that was declining in price."

The Commission also sustained NASD findings that applicants violated the Commission's net capital and books and records requirements and that the firm had permitted Brown to effect securities transactions before he became registered with the NASD as a representative of the firm.

In another case involving failure to supervise, the Commission sustained the NASD's action expelling A. J. Gabriel & Go., Inc. from membership in the Association and revoking the registration of Aaron J. Gabriel, its president and sole stockholder. It was undisputed that in a 20-month period the member confirmed as agent and charged customers commissions in 73 transactions in which the member actually had acted as principal; failed to disclose in 28 transactions that it was acting in a dual agency capacity; and failed to liquidate promptly 116 purchases by customers as to which payment was not made within 7 business days as required by Regulation T of the Federal Reserve Board. It was also undisputed that the member's books and records were not maintained in accordance with the Commission's rules and that on July 31, 1961, the member was not in compliance with the Commission's net capital rule.

The Commission also sustained NASD findings that the applicants violated the Association's interpretation with respect to "free-riding" and withholding by allocating 500 shares of the member's 2,000-share participation in a public offering of Hupp Systems, Inc. stock to the account of Gabriel's wife. Applicants contended that the NASD had failed to establish that the member had unfilled orders from the public or had failed to make a bona fide public offering. In rejecting this contention, the Commission pointed out that the stock, offered at $3 per share, was being quoted in the over-the-counter market immediately after the offering at $4 bid and $4.50 asked, and that within a week the wife had sold 400 of her shares at $3.50 and another 100 shares at $3.75 per share. The Commission concluded that "these facts lead to the inference that public purchasers were available at the time of the underwriting."

Although the applicants did not deny their failure to supervise adequately, they urged in mitigation that the violations, other than the free-riding violations, were caused by the incompetence and carelessness of back office personnel and that a rapid increase in the firm's business had forced Gabriel to spend most of his time dealing with sales and supervision of registered representatives. However, the Commission found that the violations were pervasive and representative of a general failure to supervise vital areas of the member's operations, and stated that Gabriel "should have made arrangements for additional supervision or restricted the business rather than rely completely on clerical personnel for compliance with important regulatory requirements." The Commission further held, however, that while Gabriel was not qualified to manage a broker-dealer business, the public interest did not require that he be prohibited from working in the securities business as an employee upon a showing of adequate supervision.

Other decisions of interest involved the appropriate standards for determining the fairness, under the NASD's markup policy, of prices charged by members in retail sales.

Both in C. A. Benson & Co., Inc. and Strathmore Securities, Inc. a principal issue related to the proper basis upon which to compute the amount of markups. The Commission reaffirmed its holdings in prior cases that in the absence of countervailing evidence a dealer's contemporaneous cost is the best evidence of current market price. Applicants contended that they were making wholesale markets and that the NASD should have computed the markups on the basis of their own inside offering prices, but the Commission found that they were selling the stocks in question entirely or almost entirely to retail customers and that the few sales made by the Strathmore firm to other broker-dealers were not made at its asked quotations. The Commission concluded that under these circumstances the NASD had properly disregarded those quotations. However, the Commission reversed the NASD's findings respecting 41 sales made by the Strathmore firm as to which the NASD had computed the markups based on the cost of a large block of stock. The firm purchased that block at a low price from a dealer who had sought unsuccessfully to dispose of it for some time. The Commission determined that the NASD should have based its computations on the higher prices paid to other dealers in

smaller transactions effected at about the same time and concluded that on this basis the sales prices were not unfair.

COMMISSION REVIEW OF NASD ACTION ON MEMBERSHIP

As previously noted, Section 15A (b) (4) of the Act and the by-laws of the NASD provide that, except where the Commission finds it appropriate in the public interest to approve or direct to the contrary, no broker or dealer may be admitted to or continued in membership if he, or any person associated with him, is under any of the several disabilities specified in the statute or the by-laws. A Commission order approving or directing admission to or continuance in Association membership, notwithstanding a disqualification under Section 15A (b) (4) of the Act or under an effective Association rule adopted under that Section or Section 15A (b) (3), is generally entered only after the matter has been submitted initially to the Association by the member or applicant for membership. The Association in its discretion may then file an application with the Commission on behalf of the petitioner. If the Association refuses to sponsor such an application the broker or dealer may apply directly to the Commission for an order directing the Association to admit or continue him in membership. At the beginning of the fiscal year, one application for approval of admission to or continuance in membership was pending. During the year 18 additional applications were filed, 11 were approved, 1 was withdrawn, and 2 were denied, leaving 5 applications pending at the year's end.

The Commission denied an application by the NASD that a member be continued in membership with Jerome H. Truen in its employ. The actions giving rise to Truen's disqualification occurred while he was employed as a salesman by N. Pinsker & Co., Inc. ("Pinsker") between September 1957 and March 1959, when he engaged in an intensive high-pressure telephone campaign to sell two highly speculative stocks to customers irrespective of their investment needs and objectives. [Footnote: Pinsker's broker-dealer registration was revoked for, among other things, conducting fraudulent sales activities with respect to one of these stocks.] In 1962 Truen's earlier misdeeds with the Pinsker firm formed the basis for the Commission's action denying an application by A. J. Caradean & Co., Inc. for registration as a broker-dealer and finding Truen a cause of such denial. Truen was Caradean's president and owned 50 percent of its stock.

It was contended by Truen and on his behalf that the Commission should grant the continuance application because Truen was young and inexperienced at the time of the violations and his duties with the prospective employer would be confined to the areas of mergers, acquisitions, and underwritings, where he would work in a supervised capacity.

In its opinion, the Commission referred to its earlier statement made at the time of the denial proceeding that Truen's conduct demonstrated "gross indifference to the basic duty of fair dealing required of securities salesmen." The Commission also noted the

representation made by Truen's prospective employer that Truen would not be permitted to engage in retail sales or trading, but pointed out that the standard of conduct required in other aspects of the securities business is "no less high and exacting." Under the circumstances the Commission found that Truen's prior conduct did not "inspire confidence" that he would maintain high standards of fair dealing in the area of his proposed employment. In denying the application the Commission concluded that Truen had failed to make a positive showing that his conduct since his violations had been on "such a high plane as to demonstrate that he has changed his ways."

Commission Inspections of the NASD

Under the regulatory scheme of the Exchange Act the Commission is also charged with general oversight of national securities associations in the performance of their self-regulatory activities. In carrying out this responsibility the Commission staff conducts periodic inspections of various phases of NASD activity. These inspections assist the Commission in insuring that the NASD is complying with its self-regulatory responsibilities and enable the Commission to recommend improvements designed to increase the effectiveness of such self-regulation.

During the past fiscal year, inspections were made of the entire operation of the Association's district office in Chicago and of the program of the NASD New York district office for handling public complaints. Where it appeared to the staff of the Commission that modifications of NASD procedures or policies were desirable in order to improve the Association's performance, the staff's views were communicated to the Association and conferences were held to arrive at appropriate solutions.

REVISION OF RULES, REGULATIONS AND FORMS

Parts I and II of this Report discuss several new or amended rules which were adopted or proposed during the fiscal year in connection with the implementation of the Report of the Special Study of Securities Markets and the Securities Acts Amendments of 1964. Additional revisions are summarized below.

Amendment of Rule 3a12-3

During the fiscal year the Commission adopted an amendment to Rule 3a12-3. Notice of the proposed amendment was published earlier in the year and all comments and suggestions received in response to that notice were considered in the preparation of the rule as adopted by the Commission.

Rule 3a12-3 as previously in effect exempted securities of certain foreign issuers listed on a national securities exchange and registered under Section 12 (b) of the Act from the operation of Sections 14 (a) and 16 of the Act. The amendment removes this exemption

with respect to certain equity securities and receipts and voting trust certificates therefor, if more than 50 percent of the outstanding voting securities of the issuer are held by United States residents and the business of the issuer is administered principally in the United States or 50 percent or more of the members of the board of directors are residents of the United States.

Amendments to the Proxy Rules

During the fiscal year, the Commission adopted certain amendments to its proxy rules contained in Regulation 14A under the Act which clarified the existing rules and embodied in the rules certain longstanding practices of the Commission. A limited number of substantive changes in the rules were also adopted. For example, Rule 14a-4 was amended to require that where a proxy is solicited for elections to office and for other specified matters, provision shall be made whereby the security holder may withhold authority to vote for elections to office. Rule 14a-9, which relates to false or misleading statements in proxy solicitations, was amended to state specifically that the filing of proxy material with the Commission or the examination of such material by the Commission is not to be deemed a finding by the Commission that such material is accurate or complete or not false or misleading or that the Commission has passed upon the merits of the statements contained therein or any matter to be acted upon by security holders. Item 14 of Schedule 14A specifies the information to be furnished where proxies are solicited in regard to a proposed merger, consolidation, acquisition or similar matter. The item previously required certain information to be furnished with respect to each person, other than the issuer, involved in the proposed transaction. It was amended to codify present administrative practice in requiring that such information be furnished for the issuer also in order that security holders may have a complete picture of the nature and effect of the proposed transaction. The amended item also codifies present administrative practice in requiring information with respect to the existing and pro forma capitalization and appropriate summaries of earnings on an historical and pro forma basis for the persons involved in the proposed transaction.

In addition, the scope of Item 7 (f) of Schedule 14A, calling for a description of any material interest of certain persons in transactions with the issuer, was clarified and extended.

A detailed description of all of the amendments is contained in Securities Exchange Act Release Nos. 7775 (December 22, 1965) and 7804 (January 27, 1966).

Amendment of Rule 15b6-1 and Adoption of Related Form BDW

The Commission amended Rule 15b6-1 to require that notice of withdrawal from registration as a broker-dealer be filed on a new form designated Form BDW and to provide a 60-day waiting period between the filing of the form and the effective date of withdrawal. Form BDW requires a broker-dealer seeking to withdraw to furnish specified

information: (a) whether he owes any money or securities to any customer, broker, or dealer (and if he does, he must show the amount involved and arrangements made for payment and submit a current financial statement); (b) whether he is involved in any legal actions or proceedings and whether there are any unsatisfied judgments or liens against him; (c.) the name and address of the person who will have custody or possession of his books and records required to be preserved under Rule 17a-4; and (d) the address where such books and records are located. The form also contains a consent by the withdrawing broker-dealer to make the books and records he is required to preserve available for examination by authorized members of the Commission staff and an authorization to the custodian of such books and records to make them so available.

Renumbering of Rules Under Sections 15 (b) and 15A and Amendment of Rules 15A/2-1, 17a-5, and 19a3-1 to Conform

Prior to the Securities Acts Amendments of 1964, Section 15 (b) consisted of 4 unnumbered paragraphs. As a result of those amendments the Section now consists of 10 numbered paragraphs. Therefore, the Commission renumbered its rules under Section 15 (b) to identify the specific numbered paragraph of that Section to which each rule primarily relates. In addition, to avoid confusion the Commission renumbered the rules under Section 15A by changing the initial lower case letter "a" in the designation of each of those rules to the upper case letter "A." The Commission also amended renumbered Rule 15A/2-1 and Rules 17a-5 and 19a3-1 so that the references in those rules to the renumbered rules under Section 15 (b) reflect the new designation of such rules.

Amendment of Rule 16a-2

An amendment to Rule 16a-2 adopted during the fiscal year, relating to the method of computing percentage ownership under Section 16 (a) of the Act (the insider reporting provision), was described in the 31st Annual Report.

Proposed Amendment of Rule 16a-6

During the fiscal year the Commission invited public comments on a proposed amendment of Rule 16a-6 to require the reporting of certain additional transactions under Section 16 (a) of the Act. These would include the acquisition or disposition of any put, call, spread, straddle or other option or privilege, the pledge, including the hypothecation, of a security or the release of a security from a pledge, and the loan of a security or the repayment of such a loan.

Amendment of Rule 16b-3

Rule 16b-3 exempts from Section 16 (b) of the Act (providing for the recovery of "short swing" trading profits realized by insiders) acquisitions of shares of stock (other than stock acquired upon the exercise of an option, warrant or right) by an officer or director

pursuant to a stock bonus, profit sharing, retirement, incentive, thrift, savings or similar plan, if such plan meets the conditions specified in the rule. The rule also exempts the acquisition of a "qualified" or a "restricted" stock option pursuant to a qualified or a restricted stock option plan, and a stock option pursuant to an "employee stock purchase plan" as denned in the rule.

An amendment was adopted during the fiscal year which under certain conditions excludes from the phrase "exercise of an option, warrant or right" an election to receive a cash award, payment of which is to be deferred until after termination of employment, in stock.

Amendment of Rule 16b-6

Rule 16b-6 provides an exemption from Section 16 (b) for long-term profits arising from the disposition in certain transactions of securities within 6 months after the purchase of such securities through the exercise of an option or similar right acquired more than 6 months before its exercise or pursuant to the terms' of an employment contract entered into more than 6 months before its exercise.

During the fiscal year, the Commission amended the rule to provide that the exemption shall also be available where the security acquired through the exercise of the option or right is disposed of in a transaction involving the transfer of the issuer's assets to a third person which is controlled by the issuer of the securities to be received in the exchange. In such case, "control" is to be determined by the definition in Section 368 (c) of the Internal Revenue Code of 1954.

Amendments of Rules 16b-8 and 16b-9

During the fiscal year the Commission invited public comments on proposed amendments to Rules 16b-8 and 16b-9, and, after consideration of the comments received and further consideration of the matter, adopted amendments to those rules.

The amended Rule 16b-8 provides that the acquisition and disposition of equity securities pursuant to the deposit or withdrawal of such securities under a voting trust or deposit agreement are exempt from the operation of Section 16 (b) of the Act, subject to certain conditions. It requires as a condition to the exemption that substantially all of the assets held under the voting trust or deposit agreement immediately after the deposit or immediately prior to the withdrawal consist of equity securities of the class deposited or withdrawn.

The amended Rule 16b-9 provides an exemption from Section 16 (b) for the conversion of an equity security into another equity security of the same issuer, provided that no more than 15 percent of the value of the security received at the time of the conversion is received or paid in cash or other property other than the convertible security given in

exchange. The amended rule does not apply to the exercise of an option to purchase a security.

Proposed Amendments to Forms 3 and 4

During the fiscal year, the Commission announced that it had under consideration the proposed revision of Forms 3 and 4 which are used for reporting security holdings and transactions pursuant to Section 16 (a) of the Exchange Act, Section 17 (a) of the Public Utility Holding Company Act of 1935 and Section 30 (f) of the Investment Company Act of 1940.3S Form 3 is prescribed for initial statements of beneficial ownership and Form 4 for reporting changes in such ownership.

Among other things, the amended forms would require the reporting person to list his Social Security or I.R.S. Employer Identification number, in order to provide a ready means of identification in connection with the Commission's automatic data-processing program. Amended Form 4 would provide that the price per share be reported with respect to securities bought or sold for cash, and that, with respect to securities purchased or sold otherwise than in the open market, the name and address of the seller or purchaser be given.

Proposed Amendments to Form 8-K

Certain proposed amendments to Form 8-K which were described in the 31st Annual Report were still under consideration at the close of the fiscal year.

Amendments to Forms 10, 12, 10-K and 12-K

During the fiscal year, the Commission adopted certain amendments to the instructions contained in Forms 10, 12, 10-K and 12-K. In general, the amendments relax previous requirements with respect to the disclosure required regarding the number of holders of non-transferable employee stock options and increases and decreases in such options.

Amendments to Forms 16 and 16-K

Certain proposed amendments to Forms 16 and 16-K were described in the 31st Annual Report. During the fiscal year, the Commission adopted the revised forms in the form in which they were published for comment with the exception of one change relating to the manner in which the registration statement or annual report should be signed. The revised forms provide that the document shall be signed by all of the voting trustees or by any lesser number which will legally bind all the trustees. If it is signed by less than all of the trustees it must include an opinion of counsel as to the authority of the person signing to bind the others.

Proposed Revisions of Form X-17A-5 and Minimum Audit Requirements

Proposed revisions of Form X-17A-5 (the form for the annual financial report required to be filed by brokers and dealers under Rule 17a-5) and of the minimum audit requirements under Rule 17a-5 were announced by the Commission during the year.40 The proposed changes of the form are designed to strengthen it by expanding and clarifying the requirements, especially for the benefit of the smaller broker-dealers who may have difficulty in preparing the present form. The proposed revision of the minimum audit requirements would emphasize (1) that the purpose of the audit is to enable the accountant to express an opinion on the effectiveness of the internal control and procedures for safeguarding securities as well as on the financial questionnaire, and (2) that the requirements are a minimum only and should not be interpreted as limiting or permitting the omission of any other audit procedure which may be necessary under the circumstances.

PART VI
ADMINISTRATION OF THE PUBLIC UTILITY HOLDING COMPANY ACT OF 1935

In administering the Public Utility Holding Company Act of 1935 the Commission regulates interstate public-utility holding-company systems engaged in the electric utility business and/or in the retail distribution of gas. The Commission's jurisdiction also extends to natural gas pipeline companies and other non-utility companies which are subsidiaries of registered holding companies. Although the matters under the Act dealt with by the Commission and its staff embrace a variety of intricate and complex questions of law and fact generally involving more than one area of regulation, briefly there are three principal regulatory areas. The first covers those provisions of the Act, contained principally in Section 11 (b) (l), which require the physical integration of public-utility companies and functionally related properties of holding-company systems and those provisions, contained principally in Section 11 (b) (2), which require the simplification of intercorporate relationships and financial structures of holding-company systems. The second covers the financing operations of registered holding companies and their subsidiaries, the acquisition and disposition of securities and properties, and certain accounting practices, servicing arrangements and intercompany transactions. The third includes the exemptive provisions of the Act, the provisions covering the status under the Act of persons and companies, and those regulating the right of a person affiliated with a public-utility company to acquire securities resulting in a second such affiliation. Matters embraced within this last area of regulation come before the Commission and its staff frequently. Many such matters do not result in formal proceedings and others are reflected in such proceedings only in an indirect manner when they are related to issues principally under one of the other areas of regulation.

COMPOSITION OF REGISTERED HOLDING-COMPANY SYSTEMS

At the close of the fiscal year there were 26 holding companies registered under the Act. Of these, 21 are included in the 18 holding-company systems which are herein classified as "active registered holding-company systems," 3 of the 21 being subholding utility operating companies in these active systems. The remaining 5 registered holding companies are of relatively small size and are excluded from the active holding-company systems. In the 18 active systems there are 88 electric and/or gas utility subsidiaries, 69 non-utility subsidiaries, and 35 inactive companies, or a total, including the parent holding companies and the subholding companies, of 213 system companies. The table on page 78 shows the number of active holding companies and the number of subsidiaries (classified as utility, non-utility, and inactive) in each of the active systems as of June 30, 1966, and the aggregate assets of these systems, less valuation reserves, as of December 31, 1965.

[table omitted]

SECTION 11 MATTERS IN REGISTERED HOLDING-COMPANY SYSTEMS

As reported previously, the Court of Appeals for the First Circuit disagreed with the Commission's interpretation of the phrase "loss of substantial economies" in Clause (A) of Section 11 (b) (1) and reversed the order of the Commission directing New England Electric System to divest itself of its gas properties. However, in a decision rendered on May 16, 1966, the Supreme Court of the United States sustained the Commission's position, and remanded the case to the Court of Appeals for further consideration in the light of its decision. On June 14, 1966, the Court of Appeals vacated its previous order and directed the filing of further briefs.

On December 21, 1965, immediately after its acquisition of approximately 42 percent of the outstanding common stock of United Gas Corporation, Pennzoil Company registered as a holding company under the Act. United is a gas utility company engaged in the retail distribution of natural gas principally in Louisiana, Mississippi and Texas. Pennzoil directly, and United through subsidiary companies, are also engaged in substantial non-utility businesses.

Pennzoil and United subsequently filed a plan pursuant to Section 11 (e) of the Act. Part I of the plan proposes the sale of United's gas distribution system, and Part II proposes the consolidation of Pennzoil and United. It is contemplated that after the consolidation, which is subject to Commission approval, Pennzoil's registration as a holding company will be terminated pursuant to Section 5 (d) of the Act. By order dated June 27, 1966, the Commission generally authorized the proposed sale and reserved jurisdiction with respect to the price to be paid by an acceptable purchaser for the retail distribution system.

Eastern Utilities Associates, a registered holding company, and its three public-utility subsidiary companies have filed a plan under Section 11 (e) of the Act to eliminate the public minority interests in the subsidiary companies. Hearings on the plan have been held and at the close of the fiscal year, the matter was pending for decision by the Commission.

American Gas Company, a gas utility company and a registered holding company, filed a plan for its liquidation and dissolution pursuant to Section 11 (e) of the Act. Part I of the plan proposes the sale by American to a non-affiliate company of all of its properties and assets except its holdings of 88 percent of the common stock of American Gas of Wisconsin, Inc. Part of the net proceeds are to be applied toward the retirement of its outstanding bonds and bank loans. A hearing has been held on Part I, and, at the close of the fiscal year, the matter was pending for decision by the Commission.

PROCEEDINGS WITH RESPECT TO ACQUISITIONS, SALES, AND OTHER MATTERS

The Commission approved a proposal by Northeast Utilities (formerly Western Massachusetts Companies), an exempt holding company, to acquire, pursuant to an invitation for tenders, 80 percent or more of the outstanding common stocks of The Connecticut Light and Power Company and The Hartford Electric Light Company. As a result of the tender offer Northeast acquired over 98 percent of the common stocks of each of these companies, and on June 30, 1966, it registered as a holding company under the Act. Northeast also owns 100 percent of the outstanding common stock of Western Massachusetts Electric Company.

Eastern Gas and Fuel Associates, an exempt holding company which owns all the outstanding stock of Boston Gas Company, has filed an application to acquire, pursuant to an invitation for tenders, the stock of Brockton Taunton Gas Company, a non-associate gas utility company. The management of Brockton Taunton objected to the proposed offer, and extensive hearings have been held on the application. The hearings were concluded shortly after the close of the fiscal year, and briefs are scheduled to be filed.

American Natural Gas Company and a newly organized wholly-owned subsidiary company filed an application during the fiscal year to acquire through the subsidiary substantially all the assets of Central Indiana Gas Company, a non-associate public-utility company. Hearings were held after the close of the fiscal year and briefs are scheduled to be filed.

As reported previously, the Commission denied a petition by The Alabama Electric Cooperative, Inc. for leave to intervene and for a hearing with respect to a financing proposal by Alabama Power Company, an electric utility subsidiary company of The Southern Company, a registered holding company. The Cooperative sought review and the Court of Appeals for the District of Columbia Circuit affirmed the Commission's

order. In a second case, the Commission authorized the public sale of bonds and preferred stock by Alabama Power Company and again denied a request by the Cooperative for leave to intervene and for a hearing. The Court of Appeals for the Fifth Circuit affirmed the Commission's order. The Commission denied a similar petition by the Cooperative with respect to a third financing proposal by Alabama Power Company, and the Cooperative again filed a petition for review in the Court of Appeals for the Fifth Circuit. Subsequent to the close of the fiscal year, this petition was dismissed by stipulation of the parties.

FINANCING OF ACTIVE REGISTERED PUBLIC-UTILITY HOLDING COMPANIES AND THEIR SUBSIDIARIES

During the fiscal year 1966, 11 active registered holding-company systems sold 36 issues of long-term debt and capital stock aggregating $823 million to the public and financial institutions for cash pursuant to authorizations granted by the Commission under Sections 6 and 7 of the Act. All of these issues were sold for the purpose of raising new capital.

The following table shows the amounts and types of securities issued and sold for cash by registered holding companies and their subsidiary companies during fiscal 1966:

[table omitted]

The table does not include securities issued and sold by subsidiary companies to their parent holding companies, short-term notes sold to banks, portfolio sales by any of the system companies, or securities issued for stock or assets of non-affiliated companies. These issuances and sales also require authorization by the Commission except (under Section 6 (b) of the Act) the issuance of notes having a maturity of 9 months or less where the aggregate amount does not exceed 5 percent of the principal amount and par value of the other securities of the company.

Competitive Bidding

All of the 36 issues of securities sold for cash in fiscal 1966, as shown in the preceding table, were offered for competitive bidding pursuant to the requirement of Rule 50 under the Act.

During the period from May 7, 1941, the effective date of Rule 50, to June 30, 1966, a total of 941 issues of securities with an aggregate value of $14,336 million were sold at competitive bidding under the rule. These totals compare with 233 issues of securities with an aggregate value of $2,407 million which have been sold pursuant to orders of the Commission granting exceptions from the competitive bidding requirements of the rule under paragraph (a) (5) thereof. Of the total amount of securities sold pursuant to such

orders, 128 issues with a total value of $1,924 million were sold by the issuers and the balance of 105 issues with a dollar value of $483 million were portfolio sales. Of the 128 issues sold by the issuers, 70 were in an amount from $1 to $5 million, 2 bond issues were in excess of $100 million each, and 2 stock issues totaling $36 million were issued in fiscal 1966 to holders of convertible debentures and employee stock options.

POLICY AS TO REFUNDABILITY OF BONDS

In accordance with its long-standing policy under the Act, the Commission has continued to require that bonds and preferred stock sold by registered holding companies and their subsidiaries be fully refundable at the option of the issuer upon reasonable notice and that any redemption premium be reasonable in amount. During fiscal year 1966, no companies subject to the Act took advantage of the refunding privilege.

Continuing studies made by the Commission's staff for fiscal year 1966 with respect to electric and gas utility bond issues sold at competitive bidding, whether or not subject to the Act, indicated that the presence or absence of a restriction on free refundability has not affected the number of bids received by an issuer at competitive bidding. The 31st Annual Report, pages 91-92, contains a summary of the results of an examination of all electric and gas utility bond issues (including debentures) sold at competitive bidding between May 14, 1957, and June 30, 1965, by companies subject to the Act as well as those not so subject. This study was extended to include fiscal year 1966.

During the period from May 14, 1957, to June 30, 1966, a total of 591 electric and gas utility bond issues, aggregating $13,770.9 million principal amount, was offered at competitive bidding. These included 434 refundable issues totaling $8,582.5 million principal amount, and 157 non-refundable issues totaling $5,188.4. The latter issues were all non-refundable for a period of 5 years, except one which was non-refundable for 7 years. The refundable issues thus represented 73.4 percent of the total number of issues and 62.3 percent of principal amount.

The weighted average number of bids received was 4.80 on the refundable issues and 4.30 on the non-refundable issues. The median number of bids was 5 on the refundable and 4 on the nonrefundable issues. With respect to the success of the marketing of the bond issues, an issue was considered to have been successfully marketed if at least 95 percent of the issue was sold at the syndicate price up to the date of termination of the syndicate. On this basis, 63.8 percent of the refundable issues and 61.1 percent of the non-refundable issues were successful. In terms of principal amount, 59.3 percent of the refundable issues were successful, while 59.4 percent of the non-refundable ones were successful. Extension of the comparison to include the aggregate principal amount of all issues which were sold at the applicable syndicate prices up to the termination of the respective syndicates, regardless of whether a particular issue met the definition of a successful marketing, indicates that 80.9 percent of the combined principal amount of all

the refundable issues was so sold, as compared with 80.0 percent for the non-refundable issues.26 While the overall statistics for the period from May 14, 1957, to June 30, 1966, support the Commission's policy, the staff will continue its studies of refundability provisions, particularly in light of the inconsistent marketing results in fiscal year 1966.

PART VII
PARTICIPATION OF THE COMMISSION IN CORPORATE REORGANIZATIONS UNDER CHAPTER X OF THE BANKRUPTCY ACT

The Commission's role under Chapter X of the Bankruptcy Act, which provides a procedure for reorganizing corporations in the U.S. district courts, differs from that under the various other statutes which it administers. The Commission does not initiate Chapter X proceedings or hold its own hearings, and it has no authority to determine any of the issues in such proceedings. The Commission participates in proceedings under Chapter X in order to provide independent, expert assistance to the courts, the participants, and investors in a highly complex area of corporate law and finance. It pays special attention to the interests of public security holders who may not otherwise be represented effectively.

Where the scheduled indebtedness of a debtor corporation exceeds $3 million, Section 172 of Chapter X requires the judge, before approving any plan of reorganization, to submit it to the Commission for its examination and report. If the indebtedness does not exceed $3 million, the judge may, if he deems it advisable to do so, submit the plan to the Commission before deciding whether to approve it. Where the Commission files a report, copies or a summary must be sent to all security holders and creditors when they are asked to vote on the plan. The Commission has no authority to veto or to require the adoption of a plan of reorganization.

The Commission has not considered it necessary or appropriate to participate in every Chapter X case. Apart from the excessive administrative burden, many of the cases involve only trade or bank creditors and few public investors. The Commission seeks to participate principally in those proceedings in which a substantial public investor interest is involved. However, the Commission may also participate because an unfair plan has been or is about to be proposed, public security holders are not represented adequately, the reorganization proceedings are being conducted in violation of important provisions of the Act, the facts indicate that the Commission can perform a useful service, or the judge requests the Commission's participation.

The Commission has lawyers, accountants and financial analysts in its New York, Chicago and San Francisco regional offices who are engaged actively in Chapter X cases in which the Commission has filed its appearance. Supervision and review of the regional offices' Chapter X work is the responsibility of the Division of Corporate Regulation of

the Commission, which, through its Branch of Reorganization, also serves as a field office in cases arising in the Atlanta and Washington, D.C. regional areas.

SUMMARY OF ACTIVITIES

In the fiscal year 1966, the Commission continued to maintain a high level of activity under Chapter X. During the year, the Commission entered its appearance in 13 new proceedings involving companies with aggregate stated assets of $105 million and aggregate indebtedness of approximately $109 million. These proceedings involve corporations engaged in various businesses including, among others, the construction of residential dwellings, the manufacture of aluminum and automotive products, investment in real estate and real estate mortgages, small loan and retail installment financing, motels and nursing homes, asphalt refining, and a securities broker-dealer.

During the year the Commission was a party in a total of 102 reorganization proceedings, including the new proceedings. The stated assets of the companies in all these proceedings totaled approximately $634 million and their indebtedness approximately $581 million. The proceedings were pending in district courts in 31 States and the District of Columbia, as follows: 14 in New York; 10 in Florida; 9 in California; 5 each in Arizona, Illinois, Kentucky, Michigan and New Jersey; 4 each in North Carolina, Texas and Washington; 3 each in Montana, Nevada and Pennsylvania; 2 each in District of Columbia, Colorado, Kansas, Oklahoma and South Dakota; 1 each in Arkansas, Connecticut, Idaho, Iowa, Louisiana, Maryland, Massachusetts, Minnesota, Ohio, Tennessee, Utah, Virginia and West Virginia. Proceedings involving 14 principal debtor corporations were closed during the year. Thus, at the end of the fiscal year the Commission was participating in 88 reorganization proceedings.

JURISDICTIONAL, PROCEDURAL AND ADMINISTRATIVE MATTERS

In Chapter X proceedings in which it participates, the Commission seeks to have the courts apply the procedural and substantive safeguards to which all parties are entitled. The Commission also attempts to secure judicial uniformity in the construction of Chapter X and the procedures thereunder.

In Lusk Corporation an involuntary petition under Chapter X was filed within 4 months of a preferential transfer by the debtor of a substantial portion of its property as security for an antecedent debt. The debtor, after the expiration of the 4 months, filed an answer admitting all allegations in the petition except the act of bankruptcy, and at the same time filed a voluntary petition which the court approved. The preferred creditor filed an answer and a motion to dismiss the involuntary petition. The Commission was of the view that the court should not have approved the voluntary petition when a prior

involuntary petition was pending. The Commission suggested that the court vacate its order of approval and nunc pro tunc approve the involuntary petition.

As reported previously, in Joe Newcomer Finance Company, the court initially directed the debentureholders' committee, which had solicited contributions from public investors, to return the funds to the contributors and refused to allow committee members reimbursement of expenses from these funds. Subsequently, the court modified its order to provide that the cash still on hand be returned, but that the amounts already spent to pay expenses of the committee need not be reimbursed.

In Hydrocarbon Chemicals, Inc. the Court of Appeals for the Third Circuit5 affirmed an order of the district court which disallowed a priority for the claim of a creditor who had advanced funds to the receiver in the prior Chapter XI proceeding. The court agreed with the Commission that the creditor was not entitled to a priority since the borrowing had not, as required by the Bankruptcy Act, specifically been authorized by the referee. In another appeal involving this debtor, the same court of appeals held that the Chapter X court lacked jurisdiction to enjoin a foreclosure sale of property owned by a corporation, not in reorganization, in which the debtor held a majority of the stock.

In The Sire Plan Management Corp., the district court denied a motion by the indenture trustees for the public investors who owned fractional interests in real estate leased to the debtor to direct the Chapter X trustees to surrender possession and control of these properties. The indenture trustees alleged that the filing of the Chapter X petition had terminated the leases by reason of forfeiture provisions contained therein. On appeal the Commission argued for affirmance on the ground that a Chapter X court may protect public investors by refusing to surrender properties in its custody to an indenture trustee who has failed to perform fiduciary responsibilities in connection with the properties. The court of appeals did not reach the argument of the Commission but affirmed because on the facts it appeared the indenture trustees were estopped from invoking the power of termination in the leases.

In Taylor International Corp. a claim was filed against the debtor for over $4 million, based upon (a) the alleged failure of the debtor to complete construction of five large apartment buildings, and (b) the default of the debtor in making payments on the debtor's guaranty of a minimum monthly distribution to the public limited partners in these ventures. Although the claim was filed several months after the expiration of the date set by the court for filing of claims, the court approved the allowance of a compromise claim in the amount of $1.1 million.

In both General Economics Syndicate, Inc. and G.E.C. Funding Corp., involving two related debtors, the district court entered an order, over Commission objection, substituting both reorganized companies as plaintiffs in suits brought by the trustees against the former management. The Commission had opposed the motion on the ground that Section 216 of Chapter X required that causes of action accruing to the estate should

be prosecuted by the trustee. The Commission contended that, if the reorganized companies were seeking to take over the lawsuits for the purpose of discontinuing them, as suggested in the record before the court, the proper procedure was to file a motion for an order directing the trustees to discontinue the suits.

In Yale Express System, Inc., the district court agreed with the Commission that a set-off under Section 68a of the Bankruptcy Act should not be permitted in Chapter X proceedings where it would jeopardize the chance for a successful reorganization. The Court of Appeals agreed in principle but remanded the proceeding to the district court on other grounds.

Prior to the inception of the Chapter X proceeding in respect of this same debtor, a number of present and past holders of the debtor's stock and 414 percent convertible subordinated debentures had commenced at least 16 actions in State and Federal courts against a group of defendants including the debtor, its auditors and underwriters. In these actions, allegedly brought on behalf of all persons who purchased these securities between certain dates, the plaintiffs assert that the prospectus, by which $6.5 million principal amount of the debentures and 400,000 shares of stock issued by the debtor were sold to the public in 1963, and subsequent statements and reports issued by the debtor, were false and misleading. These suits against the debtor were stayed by the reorganization court and the trustee has been substituted in place of the debtor.

The managing underwriters of the 1963 issue of debentures and stock have applied to the reorganization court for leave to file cross-claims against the trustee, contending that if they are adjudged liable in the alleged class actions, they will be entitled to indemnification from the debtor pursuant to the underwriting agreement, and that the underwriters may also be defrauded purchasers of the debtor's securities and be entitled to recover if the plaintiffs in the class actions recover. The Chapter X court issued an order fixing September 30, 1966, as the last date for the debentureholders and stockholders to file proofs of claim with the trustee. Any person who is a member of the class on whose behalf the suits have been brought must file such a claim to preserve his right to participate in awards or settlements against or by the debtor or its trustee. [Footnote: A Federal grand jury in the Southern District of New York has indicted a former vice president and the former chief accountant of the debtor for filing false 1963 annual reports of the debtor and its subsidiaries with the New York Stock Exchange and the Interstate Commerce Commission, and for mail fraud.]

In Tuba Consolidated Industries, Inc., several stockholders asserted claims for over $1.3 million based on their allegations that the debtor, prior to the Chapter X proceeding, had converted their common stock by preventing the sale of such stock. These stockholders initially had acquired the stock for investment. Relying on advice from the Commission's staff, the debtor had instructed its transfer agent not to transfer their stock because the transfer might result in a sale in violation of the registration requirements of the

Securities Act of 1933. Under a compromise approved by the court the claimants were paid $150,000 in cash and were allowed claims as creditors to the extent of $225,000.

In Food Town, Inc., the Protective Committee for Preferred Shareholders filed a proof of claim on behalf of all preferred stockholders alleging false statements and material omissions in the offering circular pursuant to which the stock was sold to the public under Regulation A. Because of the debtor's insolvency, the plan of reorganization, confirmed in 1960, provided no participation for stockholders as such. The compromise approved by the court provided a modest sum for distribution, pro rata, to non-management preferred shareholders who filed proofs of claim within the time specified by the court, but in no event was any stockholder to receive more than the price he had paid for his stock.

TRUSTEE'S INVESTIGATION

A complete accounting for the stewardship of corporate affairs by the prior management is a requisite under Chapter X. One of the primary duties of the trustee is to make a thorough study of the debtor to assure the discovery and collection of all assets of the estate, including claims against officers, directors, or controlling persons who may have mismanaged the debtor's affairs.

In Hydrocarbon Chemicals, Inc., the trustee instituted a plenary action against the Bank of Commerce of New York and officers and directors of the debtor and others to recover over $2 million, alleging that the debtor was defrauded in the issuance of its stock.

In Continental Vending Machine Corp., the trustee brought suit against the former management and directors of the debtor, its accountants and others, seeking $41 million in damages to the debtor. The court authorized the trustee to compromise the lawsuit against one of the defendants, Meadow Brook National Bank, for $150,000 in cash and the release by the bank of claims against the estate of about $1.8 million. [Footnote: The debtor's former president and chairman of the board and others were indicted by a Federal grand jury on charges of mail fraud and securities law-violations based upon alleged misappropriation of vast sums from the debtor for their own use between 1958 and 1963.]

In Swan-Finch Oil Corp., the trustee received $175,000 in settlement of an action for alleged fraudulent transfer of certain assets of the debtor by Lowell M. Birrell, the former president of the debtor. The assets had been placed in receivership and upon settlement with the transferee of the property the action was discontinued.

REPORTS ON PLANS OF REORGANIZATION

Generally, the Commission files a formal advisory report only in a case involving a substantial public investor interest and presenting significant problems. When no such formal report is filed, the Commission may state its views briefly by letter, and authorize its counsel to make an oral or written presentation to amplify the Commission's views. During this fiscal year the Commission published one formal advisory report.

In F. L. Jacobs Co. the plan of reorganization provided for the internal reorganization of the debtor and the continuation of the debtor's business. Under the plan, the reorganized company was to assume all debts and obligations incurred by the trustees during the proceeding. The plan provided for a distribution of debentures and cash to the preferred stockholders, with the present common stock to remain outstanding. The preferred stockholders were to receive 6 percent debentures in the aggregate principal amount of $2,706,350, such amount being equal to the involuntary liquidation preference of $50 per share on the outstanding preferred stock exclusive of dividend arrearages. Dividend arrears of about $1 million on the preferred stock were to be paid in cash, substantially from the proceeds of a $1 million bank loan. The debentures were to mature in 15 years from the date of issue and under the proposed indenture the reorganized company would deposit 40 percent of its annual net income in a sinking fund for retirement of debentures by purchase in the open market, solicitation of tenders or redemption. No dividends could be paid on the common stock until one-half of the principal amount of debentures was redeemed or otherwise retired, or the $1 million bank loan was paid in full, whichever occurred first.

The Commission concluded that the plan was feasible and would be fair and equitable if it were amended to remove the dividend restriction on the common stock.2The court agreed with the Commission and the trustees amended the plan and as so amended the plan was approved and confirmed.

In Muskegon Motor Specialties Co., reported previously, the district court, after rehearing, reaffirmed its previous finding that the debtor was insolvent and that stockholders were not entitled to participate under the plan. The Commission supported an appeal by the preferred stockholders' committee. After the close of the fiscal year, the Court of Appeals for the Sixth Circuit affirmed, holding that the district court's determination of insolvency "was supported by substantial evidence and is not clearly erroneous."

In Rocky Mountain Chemical Corp., the court approved a plan of reorganization which provided for the sale of the assets to a new company formed by a stockholders' committee, which raised funds from the sale of stock pursuant to a Regulation A offering. The debtor had been found insolvent and the amount paid by the stockholders' committee was sufficient only to pay the expenses of administration.

In Edward N. Siegler & Co. a registered broker-dealer which was a member of the Midwest Stock Exchange filed a petition for reorganization in Cleveland, Ohio on May

23, 1966. With the assistance of the Commission, an agreement was worked out which provided for the satisfaction of the claims of all customers in full by the transfer of the customers' accounts to Hartzmark & Co., Inc., a Cleveland broker-dealer. Hartzmark has undertaken to honor all of the customers' paid security positions and free credit balances. This agreement was approved by the court on August 1, 1966. The assets held by the debtor for customers were approximately $160,000 short of the amount required to satisfy these liabilities. The Midwest Stock Exchange contributed $135,000 towards the deficiency and Hartzmark provided the balance.

In Twentieth Century Foods Corp., the Commission objected to the petition of the trustee to sell the assets of a wholly-owned subsidiary of the debtor, which constituted the major asset of the estate, unless a sale were made pursuant to a plan of reorganization. The trustee thereupon agreed to incorporate the offer to purchase the assets into a proposed plan.

In TMT Trailer Ferry Inc., as reported previously, the Stockholders' Protective Committee appealed from the order of the district court confirming an internal plan of reorganization. While the district court denied the objections of the Commission to consummation of the plan pending ultimate determination of the issues on appeal, the court accepted the suggestion of the Commission that the new common stock to be issued to creditors bear a legend disclosing the pendency of the appeal. After the close of the fiscal year, the court of appeals rendered its decision affirming the order of the district court.

ACTIVITIES WITH REGARD TO ALLOWANCES

Every reorganization case ultimately presents the difficult problem of determining the allowance of compensation to be paid to the various parties for services rendered and for expenses incurred in the proceeding. The Commission, which under Section 242 of the Bankruptcy Act may not receive any allowance for the services it renders, has sought to assist the courts in assuring economy of administration and in allocating compensation equitably on the basis of the claimants' contributions to the administration of estates and the formulation of plans. During the fiscal year 197 applications for compensation totaling about $6.9 million were reviewed.

In Automatic Washer Company the court disagreed with the view of the Commission that no compensation or reimbursement of expenses should be allowed a fee applicant in connection with the preparation of his application for an allowance or attendance at the hearing on his application. The court said that the preparation of a fee application and attendance at a hearing thereon in a Chapter X proceeding may require a substantial amount of time, which would be considered in making an allowance for fees.

In General Economics Syndicate, Inc., application for final allowances totaled $276,000, the Commission recommended $136,000, and the district court allowed $160,500. On appeal, the court reduced the allowances to the trustees and their counsel to the amount recommended by the Commission and agreed with the Commission that the allowance to counsel for certain stockholders was so low as to constitute an abuse of discretion. Counsel for the stockholders had requested $25,000, the Commission recommended $15,000, and the district court awarded $3,500. The court of appeals allowed $10,000. The court of appeals stressed the necessity for attorneys who expect to obtain an allowance to keep accurate time records.

In Swan-Finch Oil Corporation, 20 applicants requested a total of about $1,204,000 in final allowances. The Commission recommended a total of about $760,000. The Commission's recommendations were adopted by the court, except for allowance to the trustee. The latter had requested $650,000, the Commission had recommended $450,000, and the district court allowed $490,000.

In Tucker Corporation, a proceeding in which the Commission was not participating, the Commission informed the attorney for the trustee that final allowances to four law firms had been approved by the court on the basis of applications which had understated the amounts previously received by these firms as interim allowances. All four firms admitted having received interim payments which they did not report to the court at the time they applied for final allowances, but sought court approval to correct the record to show the amounts actually received as interim allowances.

The Commission moved for leave to file its appearance in the Chapter X proceeding and urged that the court order the return by the four firms of the full amount of the excess payments received by them, plus interest. The Commission also suggested that there should be an inquiry as to the circumstances surrounding the overpayments. The court denied the Commission's motion to enter the proceeding and granted the motion of the four law firms to correct the record, finding that the inaccuracies in the petitions for fees "were the result of inadvertent and honest mistakes." As a result, two of the firms actually received payments in excess of the total originally requested.

INTERVENTION IN CHAPTER XI PROCEEDINGS

Chapter XI of the Bankruptcy Act provides a procedure by which debtors can effect arrangements with respect to their unsecured debts under court supervision. Where a proceeding is brought under that chapter but the facts indicate that it should have been brought under Chapter X, Section 328 of Chapter XI authorizes the Commission or any other party in interest to make application to the court to dismiss the Chapter XI proceeding unless the debtor's petition is amended to comply with the requirements of Chapter X, or a creditors' petition under Chapter X is filed.

In Imperial "400" National, Inc. a company engaged in the business of developing and operating motels on a co-ownership basis proposed an arrangement under Chapter XI whereby the interests of the 850 common stockholders were to be eliminated and the estimated several hundred holders of the $994,000 of convertible debentures were to receive 50 percent of the stock of the reorganized company. The Commission's motion under Section 328 was based on the major adjustment of the rights of the debenture holders and the fact that the debtor was attempting a comprehensive reorganization under Chapter XI rather than a simple composition of its unsecured debts. The court agreed with the Commission's position and granted the motion stating, among other things, that there was a need for the appointment of a disinterested trustee with broad powers of investigation and for the assistance of the Commission. The debtor subsequently amended its petition to comply with Chapter X.

In American Guaranty Corporation, reported previously, the district court affirmed its previous denial, in 1963, of the Commission's Section 328 motion, which was again before the district court on remand from the Court of Appeals for the First Circuit. The Commission advised the court of appeals, which had retained jurisdiction over the matter, that it did not desire to press its appeal further and the court of appeals dismissed the appeal.

In First Mortgage Corp. of Stuart, the debtor, on the complaint of the Florida Securities Commission, had been placed in a State court receivership together with several other corporations alleged to be related to or affiliated with the debtor, including Tower Credit Corporation. A few days thereafter the debtor filed a petition under Chapter XI. This Commission's motion under Section 328, joined in by the Florida Securities Commission and many attorneys representing public investors, was denied without prejudice. Shortly thereafter the court adjudicated the debtor bankrupt. Several months later an involuntary petition under Chapter X was filed by three purported creditors against Tower, which the court dismissed on the ground that the petitioning creditors did not have valid claims. After the close of the fiscal year, three different creditors filed another involuntary Chapter X petition against Tower.

PART VIII
ADMINISTRATION OF THE TRUST INDENTURE ACT OF 1939

The Trust Indenture Act of 1939 requires that bonds, notes, debentures and similar securities publicly offered for sale, except as specifically exempted by the Act, be issued under an indenture which meets the requirements of the Act and has been duly qualified with the Commission. The Act requires that indentures to be qualified include specified provisions which provide means by which the rights of holders of securities issued under such indentures may be protected and enforced. These provisions relate to designated standards of eligibility and qualification of the corporate trustee to provide reasonable

financial responsibility and to minimize conflicting interests. The Act outlaws exculpatory provisions formerly used to eliminate all liability of the indenture trustee and imposes on the trustee, after default, the duty to use the same degree of care and skill in the exercise of the rights and powers vested in it by the indenture as a prudent man would use in the conduct of his own affairs.

The provisions of the Trust Indenture Act are closely integrated with the requirements of the Securities Act. Registration pursuant to the Securities Act of securities to be issued under a trust indenture subject to the Trust Indenture Act is not permitted to become effective unless the indenture conforms to the requirements of the latter Act, and necessary information as to the trustee and the indenture must be contained in the registration statement. In the case of securities issued in exchange for other securities of the same issuer and securities issued under a plan approved by a court or other proper authority which, although exempted from the registration requirements of the Securities Act, are not exempted from the requirements of the Trust Indenture Act, the obligor must file an application for the qualification of the indenture, including a statement of the required information concerning the eligibility and qualification of the trustee.

[table omitted]

REVISION OF RULES, REGULATIONS AND FORMS

Adoption of Rule 7a-9

During the fiscal year, the Commission adopted a new Rule 7a-9 which provides for the filing with an application for the qualification of an indenture under the Act, or as an amendment to such an application which has not become effective, of an amendment which will delay the effectiveness of the application until the 20th day after a superseding amendment is filed, or until the Commission upon request accelerates the effective date. The purpose of the new rule is to make it unnecessary to file successive delaying amendments to such applications.

Amendments to Forms T-1 and T-2

Forms T-1 and T-2 are prescribed for statements of eligibility and qualification of corporations or individuals, respectively, designated to act as trustees under indentures qualified under the Act. During the fiscal year, the Commission amended these forms to clarify and simplify them in certain respects, to delete certain required information deemed not essential to a determination of the eligibility and qualifications of the trustee, to require certain additional information deemed significant, and to bring the forms in line with the format of the Commission's more recently adopted forms under other acts.

PART IX
ADMINISTRATION OF THE INVESTMENT COMPANY ACT OF 1940

The Investment Company Act of 1940 provides for the registration and regulation of companies primarily engaged in the business of investing, reinvesting, owning, holding, or trading in securities. The Act, among other things, requires disclosure of the financial condition and investment policies of such companies; prohibits changing the nature of their business or their investment policies without shareholder approval; regulates the means of custody of the companies' assets; requires management contracts to be submitted to security holders for approval; prohibits underwriters, investment bankers, and brokers from constituting more than a minority of the directors of such companies; and prohibits transactions between such companies and their officers, directors, and affiliates except with approval of the Commission. The Act also regulates the issuance of senior securities and requires face-amount certificate companies to maintain reserves adequate to meet maturity payments upon the certificates.

The securities of investment companies which are offered to the public are also required to be registered under the Securities Act of 1933 and the companies must file periodic reports. Such companies are also subject to the Commission's proxy rules and certain "insiders" of closed-end companies are subject to reporting and "short swing" trading rules. In November 1964, certain functions relating to investment companies were reallocated from the Division of Corporation Finance to the Division of Corporate Regulation, including the administration of the disclosure requirements with respect to registration statements filed by such companies under the Securities Act of 1933 and the administration of the periodic reporting, proxy solicitation and other provisions of the Securities Exchange Act of 1934 with respect to registered investment companies. On the basis of the experience since the transfer of functions, the resulting concentration of responsibility in the Division of Corporate Regulation for the administration of the securities laws as they apply to investment companies has been of material convenience to registrants and other persons concerned with investment companies.

COMPANIES REGISTERED UNDER THE ACT

As of June 30, 1966, there were 775 investment companies registered under the Act, including 70 small business investment companies. Of this total, 667 were "active" companies, whose assets had an aggregate market value of approximately $49.8 billion. Compared with the corresponding totals at June 30, 1965, these figures represent an overall increase of approximately $5.2 billion in the market value of assets and an increase of 51 in the number of active registered companies. The asset increase is partly due to the appreciation in assets of previously registered companies and partly to the large increase in the number of registered companies. The classification of the registered

companies and the approximate market value of the assets in each category as of June 30, 1966, are shown in the following table:

[table omitted]

"Inactive" refers to registered companies which, as of June 30, 1966, were in the process of being liquidated or merged, or have filed an application pursuant to Section 8 (f) of the Act for deregistration, or which have otherwise gone out of existence and remain registered only until such time as the Commission issues orders under Section 8 (f) terminating their registration.

The approximately $4 billion of assets of the "active" registered unit investment trusts include approximately $3.5 billion of assets of registered unit investment trusts which invest in securities of other registered investment companies, substantially all of them management open-end companies.

During the fiscal year, 78 new companies, including 5 small business investment companies, registered under the Act while the registrations of 30 companies, including 3 small business investment companies, were terminated. The classification of these companies is as follows:

[table omitted]

GROWTH OF INVESTMENT COMPANY ASSETS

The following table illustrates the striking growth of assets of investment companies over the years since the enactment of the Investment Company Act:

[table omitted]

INSPECTION AND INVESTIGATION PROGRAM

During fiscal year 1966, 152 investment company inspections were completed pursuant to Section 31 (b) of the Act. Many of the inspections disclosed violations not only of the Investment Company Act but also of other statutes administered by the Commission. A number of the violations uncovered during routine inspections were serious in nature. They included failure to observe the procedures which had been established for safekeeping of the company's assets, and failure to disclose the true sources of periodic income dividends and capital gain distributions paid to shareholders. The inspections also disclosed several situations in which the procedures for pricing shares for purposes of purchase or redemption did not conform with statutory requirements or with the procedure set forth in the company's prospectus. The inspections further uncovered a

number of instances in which self-dealing transactions had been effected by affiliated persons in violation of Section 17 of the Act.

Largely as an outgrowth of information obtained during routine inspections, 17 private investigations were commenced during the fiscal year to develop the facts concerning what appeared to be serious violations of the statutes administered by the Commission.

On the basis of the facts obtained in private investigations, three civil actions were instituted by the Commission during the fiscal year 1966. One action sought, among other things, to enjoin an investment company and its officers and agents from issuing, selling, purchasing, or redeeming any securities while it failed to maintain and keep current its books and records. The action further sought appointment of a conservator for the company's assets to protect the interests of shareholders. In another action the Commission obtained a preliminary injunction restraining a company and its wholly-owned subsidiaries from doing business as unregistered investment companies in violation of the Act. This action further seeks to enjoin affiliated persons from engaging in transactions which, had the company been registered, would have been prohibited by Section 17 (a) of the Act. The complaint also alleges that certain defendants caused the filing of false reports with the Commission. In the third action the Commission seeks to enjoin certain affiliated persons of a registered investment company from effecting self-dealing transactions with the investment company, and alleges gross abuse of trust and gross misconduct within the meaning of Section 36 of the Act.

As a result of an investigation by the Commission, Herman I. Weiner, former secretary of Revere Fund, Inc., a registered investment company, was charged in a criminal information in the Eastern District of Pennsylvania with conversion and embezzlement of the company's assets and transmitting a materially false and misleading letter to the Commission with respect to his activities. Weiner entered a plea of nolo contenders, and is to be sentenced at a later date.

As a result of the Commission's inspection and investigation program, approximately $316,000 was returned to investors either directly or indirectly during the 1966 fiscal year. The major portion of this recovery resulted from a court-approved settlement in an injunctive proceeding instituted by the Commission, involving Electro-Science Investors, Inc. Under the terms of the settlement, a former director of this investment company agreed to pay $225,000 to the company. The injunctive action had stemmed largely from the director's personal transactions in a security which was also included in the company's portfolio. In addition, the Commission settled several matters out of court with resulting benefits to investors.

ANNUAL REPORTING BY MANAGEMENT INVESTMENT COMPANIES

During the fiscal year, the initial annual reports to the Commission by registered management investment companies on the revised reporting form, captioned N-1R, were utilized by the Division of Corporate Regulation in the examination of investment company matters, including the program of inspection and enforcement. The reports have been of substantial assistance in the processing of investment company filings, the inspection of investment companies, and the disclosure of violations of the Act. They provide considerable savings in time and expense by making available information relating to individual companies which could otherwise only be obtained through more frequent and detailed inspections. The reports also enable the Commission to develop information on various industry practices as an important aid to the exercise of the Commission's responsibilities under the statute.

FILINGS REVIEWED

As previously noted, investment companies offering their shares for sale to the public must register them under the Securities Act of 1933. The companies themselves, of course, must register under the Investment Company Act. The registration statements of investment companies filed pursuant to the Securities Act are reviewed for compliance with that Act and the Investment Company Act. The Commission's rules promulgated under the Investment Company Act generally require that the basic information contained in notifications of registration and in registration statements of investment companies filed under the Investment Company Act be kept current through periodic and other reports. In addition, proxy soliciting material filed by investment companies is reviewed for compliance with the Commission's proxy rules. The following table sets forth the nature and volume of filings processed during the past fiscal year:

[table omitted]

APPLICATIONS AND PROCEEDINGS

Under Section 6 (c) of the Act, the Commission, by rules and regulations, upon its own motion or by order upon application, may exempt any person, security, or transaction from any provision of the Act if and to the extent 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 the Act. Other Sections, such as 6 (d), 9 (b), 10 (f), 17 (b), 17 (d), and 23 (c), contain specific provisions and standards pursuant to which the Commission may grant exemptions from particular sections of the Act or may approve certain types of transactions. Also, under certain provisions of Sections 2, 3, and 8, the Commission may determine the status of persons and companies under the Act. One of the principal activities of the Commission in its regulation of investment companies is the consideration of applications for orders under the sections referred to.

During the fiscal year, 213 applications filed under various sections of the Act were before the Commission, and 183 applications were disposed of. As of the end of the year, 100 applications were pending. The sections of the Act with which these applications were concerned and the disposition of applications are shown in the following table:

[table omitted]

Some of the more significant matters in which applications were considered are summarized below:

On March 9, 1966 the Commission, with one Commissioner dissenting, issued its opinion and order granting in part, and denying in part, an application filed pursuant to Section 6 (c) of the Act by First National City Bank of New York requesting exemptions from certain provisions of the Act, principally Sections 10 (b) (3), 10 (c), and 10 (d) (2), with respect to a Commingled Investment Account ("Account") which the Bank proposed to establish and to register under the Act as a diversified open-end management investment company.

The Bank's application proposed that the Account would operate as a collective investment fund pursuant to regulations of the Comptroller of the Currency and accept investments of $10,000 or more pursuant to agreements between investors and the Bank. No sales load would be imposed. The Bank would serve as investment adviser for the Account, subject to investor approval. The operation of the Account was to be subject to the supervision of a Committee of at least three persons, at least one of whom would be unaffiliated with the Bank. The Commission denied an exemption from Section 10 (d) (2) of the Act. This exemption would have permitted all but one of the members of the Committee, which would be equivalent to a board of directors, to be affiliated with the Bank. However, the Commission granted exemptions from Sections 10 (b) (2), 10 (b) (3), and 10 (c) of the Act, which provide in substance that the majority of the board of directors of a registered investment company may not be (a) affiliated with the principal underwriter of the investment company, (b) affiliated with an investment banker, or (c) officers or directors of any one bank. The effect of the exemptions granted by the Commission was thus to permit a majority of the Committee to consist of officers or directors of, or persons otherwise affiliated with, the Bank. The Account remains subject to Section 10 (a) of the Act, under which not more than 60 percent of the members of the Committee may consist of persons who are affiliated with the Bank.

In granting the exemptions, the Commission stressed, among other things, that the Account differed substantially from the bank-dominated investment companies with which Congress was concerned in enacting Section 10 (c) and that there were substantial safeguards against conflicts of interest which could arise as a result of the Bank's commercial banking activities.

Commissioner Budge, dissenting from the Commission's decision, stated that the granting of the exemptions was contrary to the expressed statutory prohibition against bank domination of investment companies. He referred to the statutory history which indicated conflicts and potential conflicts of interest between a bank and the investment company it dominates. He expressed the view that if the restrictions of Section 10 (c) are to be avoided, this should be accomplished through legislation and not through ad hoc exemptions, particularly when, as here, the Commission and the bank regulatory agencies have adopted contrary interpretations as to the very nature of the proposed investment company.

The National Association of Securities Dealers, Inc. which appeared in opposition to the Bank's application, has filed a petition to review the Commission's order in the Court of Appeals for the District of Columbia Circuit. The Investment Company Institute, which also opposed the application, filed a complaint in the District Court for the District of Columbia against the Comptroller of the Currency seeking, among other things, to enjoin his approval of the Bank's plan.

On May 6, 1966, the Commission released its Findings and Opinions and Order in Electric Bond and Share Company. This opinion denied the application of Electric Bond and Share Company ("Bond and Share") for an order pursuant to Section 8 (f) of the Act declaring that it had ceased to be an investment company and also denied Bond and Share's alternative applications pursuant to Section 3 (b) (2) of the Act for an order declaring that it is not primarily engaged in the business of an investment company and, pursuant to Section 6 (c) of the Act, for an order exempting it from the Act. The Commission also denied the application of American & Foreign Power Company Inc. ("Foreign Power"), a majority-owned subsidiary of Bond and Share, for an order pursuant to Section 3 (b) (2) of the Act declaring that Foreign Power is not an investment company, or alternatively, for an order exempting it from the Act pursuant to Section 6 (c).

In rejecting the applications, the Commission stated that obligations of foreign countries, which Foreign Power had received in exchange for various of its foreign utility interests, are investment securities as that term is used in the Act. Such securities constituted over 80 percent of Foreign Power's assets from which it derived about 76 percent of its income. Therefore, the Commission held that Foreign Power was no longer primarily engaged in utility operations and that it was not entitled to exemption from the Act. In addition, the Commission held that Bond and Share was not entitled to exemption from the Act since about two-thirds of its assets from which it derived about 60 percent of its income consisted of marketable investment securities and securities of Foreign Power.

On May 11, 1966, the Commission issued its opinion and order denying motions to dismiss an application filed pursuant to Section 2 (a) (9) of the Act by Randolph Phillips, a stockholder of four investment companies for which Investors Diversified Services, Inc. ("IDS") serves as investment adviser and principal underwriter, and denying the control

determinations sought by Phillips. In refusing to dismiss the application, the Commission, adhering to the conclusions reached by it in Fundamental Investors, Inc., held that a shareholder of a registered investment company is an "interested person" within the meaning of Section 2 (a) (9) of the Act and entitled to file with the Commission an application for an order that, contrary to the presumptions contained in that section, a person or group of persons are in control of an investment company's adviser and the company controlling such adviser, and that the Commission may make a determination relating to a period preceding such determination.

Phillips' application alleged that in 1962 Bertin C. Gamble and two affiliated companies had acquired control of Alleghany Corporation, which controls IDS, and of IDS. The Commission concluded, however, that the presumption under Section 2 (a) (9) of the Act that the Gamble group, as the owner of less than 25 percent of Allegheny's stock, did not control that company had not been rebutted. In October 1962, John D. Murchison and Clint W. Murchison, Jr. and their associates, who had gained control of Alleghany in a 1961 proxy contest, sold 15 percent of the voting stock of Alleghany to the Gamble group and granted that group a right to purchase an additional 15-20 percent and to assume 2 seats on the 10-man board of directors. However, the Gamble group failed to reach an accord with Alan P. Kirby, Sr., a 33 percent stockholder of Alleghany who was engaged in efforts to regain control of Alleghany, and its contemplated succession to the Murchison group's holdings and positions did not materialize. The Commission also found that the record did not establish the existence of a claimed secret agreement between the Murchison and Gamble groups to transfer control to the latter or show that certain actions of Alleghany and IDS were attributable to the controlling influence of the Gamble group. Phillips has filed a petition for review in the Court of Appeals for the Second Circuit.

At the close of the fiscal year there were pending for determination by the Commission two proceedings involving the issuance of stock options. In one of these cases, State Bond & Mortgage Company, a registered face-amount certificate company, was seeking authorization for certain stock options theretofore issued, and to be issued, under a stock option plan for its officers and employees. Section 18 (j) of the Act prohibits a face-amount certificate company from issuing any security, except in accordance with Commission authorization thereunder, other than (i) a face-amount certificate, (ii) a non-preference voting common stock, and (iii) short term, privately issued indebtedness. It also prohibits the issuance of any securities except for cash or securities.

In the other proceeding, the Variable Annuity Life Insurance Company of America ("VALIC"), a registered open-end management investment company, sought an exemption under Section 6 (c) of the Act for the proposed issuance of stock options under a stock option plan for its officers and employees. Section 18 (d) of the Act, with certain inapplicable exceptions, prohibits a registered management investment company from issuing any warrant or right to subscribe to a security of which it is the issuer. Section 22 (g) of the Act as applicable prohibits a registered open-end investment company from

issuing any of its securities for services or for property other than cash or securities. Subsequent to the close of the fiscal year, the Commission denied both applications.

REVISION OF RULES, REGULATIONS AND FORMS

Proposed Rule 17a-7

During the fiscal year, the Commission invited public comments on proposed Rule 17a-7 to exempt certain purchase or sale transactions between affiliated registered investment companies from the provisions of Section 17 (a) of the Act. That section prohibits an affiliated person of a registered investment company or an affiliated person of such a person, acting as principal, from knowingly selling to or purchasing from the investment company or a company controlled by the investment company any security or other property, unless the Commission grants an exemption. The proposed rule would exempt transactions involving a security traded on a national securities exchange and effected at a price determined in accordance with the provisions of the rule. The exemption would be available only where the transaction is consistent with the policy of each registered investment company, as recited in its registration statement and reports filed under the Act, and where no brokerage commission, fee or other remuneration is paid in connection with the transaction, except for customary transfer fees.

PART X
ADMINISTRATION OF THE INVESTMENT ADVISERS ACT OF 1940

The Investment Advisers Act of 1940 established a pattern of regulation of investment advisers similar to that contained in the Securities Exchange Act with respect to the conduct of broker-dealers. With certain specific exceptions, the Act requires persons engaged for compensation in the business of advising others with respect to securities to register with the Commission and to conform to statutory standards designed to protect the public interest. The Act prohibits fraudulent conduct, and authorizes the Commission to define, and prescribe means reasonably designed to prevent fraudulent, deceptive or manipulative acts or practices. Pursuant to such authority, Rule 206 (4)-1 proscribes, among other things, the use of testimonials, circumscribes permissible references to past recommendations and the use of graphs and charts, and prohibits the use of false or misleading statements. Under Rule 206 (4)-2, an investment adviser who has custody or possession of the funds or securities of clients must segregate them, maintain them in the manner provided in the rule and comply with certain other conditions.

The Act prohibits an investment adviser from basing his compensation upon a share of the capital gains or appreciation of his client's funds, and prohibits the assignment of investment advisory contracts without the client's consent. Advisers are also required to

make, keep and preserve books and records in accordance with the Commission's rules and the Commission is empowered to conduct inspections of such books and records.

Investment advisers who violate any of the provisions of the Act or of the rules thereunder are subject to appropriate administrative, civil or criminal sanctions. The Act provides, in Section 203 (d), that the Commission shall deny, revoke, or suspend for not more than 12 months, the registration of an investment adviser if it finds that such action is in the public interest and that the investment adviser or any partner, officer, director or controlling or controlled person of the investment adviser is subject to a specified disqualification. These disqualifications include wilful misstatements in an application or report filed with the Commission, the existence of a conviction or injunction based on or related to specified types of misconduct, willful violation of any provisions of the Securities Act, Securities Exchange Act or Investment Advisers Act or any rule or regulation thereunder, and aiding and abetting any other person's violation of such provisions, rules or regulations. In addition, the Commission may seek injunctions to restrain violations of the Act and may recommend criminal prosecution by the Department of Justice for fraudulent misconduct or wilful violation of the Act or the Commission's rules thereunder.

Registration Statistics

At the close of the fiscal year 1,633 investment advisers were registered with the Commission. The following tabulation contains other statistics relating to registrations and applications for registration:

[table omitted]

Inspection Program

During fiscal 1966, 251 inspections of investment advisers were completed by the Commission's staff (as compared to 260 the preceding year). These inspections disclosed a total of 151 indicated violations of the Act and the rules and regulations promulgated thereunder, as reflected in the following table:

[table omitted]

Administrative Proceedings

Set forth below are statistics with respect to administrative proceedings under the Investment Advisers Act which were pending during fiscal year 1966:

[table omitted]

REVISION OF RULES, REGULATIONS AND FORMS

Amendment of Rule 204-2 (a)

During the fiscal year the Commission invited comments on a proposed amendment of Rule 204-2 (a) to require investment advisers to maintain records containing specified information concerning securities transactions in which they or certain of their personnel have any beneficial interest. Shortly after the end of the year the amendment was adopted. The background and significance of this amendment are discussed in Part I of this Report.

PART XI
OTHER ACTIVITIES OF THE COMMISSION

CIVIL LITIGATION

The several statutes administered by the Commission authorize the Commission to seek injunctions against continuing or threatened violations of such statutes. Such violations may involve a wide range of illegal practices, including the purchase or sale of securities by fraud, and the sale of securities without compliance with the registration requirements of the Securities Act. The Commission also participates in various other types of proceedings, including appearances as amicus curiae in litigation between private parties where it is important that its views regarding the interpretation of the statutory provisions involved be furnished to the court, corporate reorganization proceedings under Chapter X of the Bankruptcy Act, and various types of civil appellate proceedings.

Tables 10 and 12 in the appendix to this report contain statistics with respect to the various types of civil proceedings in which the Commission participated prior to and during the fiscal year. A summary of injunction proceedings instituted by the Commission since 1934 may be found in Table 11. This section describes a few of the more noteworthy cases which were pending during the fiscal year, not including, however, cases arising under the Public Utility Holding Company Act or Chapter X of the Bankruptcy Act; such cases are discussed in the sections of this report dealing with those statutes.

In an important decision involving the scope of the "insurance" exemptions to the disclosure and regulatory provisions of the Securities Act of 1933 and the Investment Company Act of 1940, the Court of Appeals for the District of Columbia Circuit, in S.E.C.. v. United Benefit Life Insurance Co. affirming the decision of the district court, held that the "Flexible Fund Annuity" offered and sold by the United Benefit Life Insurance Company is a contract of insurance and therefore exempt from the coverage of

the 1933 and 1940 Acts by virtue of the statutory exemptions relating to insurance and annuities.

The Commission had urged that the insurance exemptions were unavailable because the Flexible Fund contract is offered and promoted as a vehicle for investing in the stock market and because the purchaser's fortunes during the pay-in period, when he is a participant in the Flexible Fund, are, to a substantial extent, directly dependent on the investment experience of a portfolio of securities managed by the company. The court of appeals, rejecting the Commission's position, held that the exemptions were available, because (1) under the minimum guarantee the company has assumed a substantial part of the investment risk during the pay-in period, and (2) the company has assumed the major part of the investment risk over the duration of the entire contract including both pay-in and pay-out periods. After the close of the fiscal year the Supreme Court granted a petition for certiorari filed by the Commission.

In Kaplan v. Lehman Brothers a derivative action on behalf of certain investment companies seeking injunctive relief and treble damages against the New York Stock Exchange and several member firms for alleged violations of the anti-trust laws in fixing minimum commission rates for transactions on the Exchange, the district court, relying on Silver v. New York Stock Exchange, held that the Exchange's commission rate rules did not violate the anti-trust laws, since such rules were specifically contemplated under the regulatory scheme of the 1934 Act. The court further held that determination of the reasonableness of the Exchange's rates should be left to the prospective decisions of the Commission. Plaintiffs have appealed to the Court of Appeals for the Seventh Circuit and that court has granted the Commission leave to participate as amicus curiae.

In Fifth Avenue Coach Lines, Inc. v. New York Stock Exchange the Appellate Division of the New York Supreme Court unanimously reversed the lower court which had denied the Exchange's motion to dismiss an action brought by Fifth Avenue Coach Lines, Inc. to enjoin the Exchange from delisting its stock. Fifth Avenue had alleged that such delisting would be arbitrary and harmful to the interests of stockholders. The Exchange had applied to the Commission to delist the stock. Adopting the position of the Commission, amicus curiae, the court held that the State court lacked jurisdiction of the subject matter of the action in that the Securities Exchange Act of 1934 provides the exclusive procedure for delisting securities and such procedure constitutes a pre-emption of the area by the Federal Government. The court stated that the "statutory provisions constitute an integrated administrative and judicial procedure by which, it seems clear. Congress intended the delisting process to be specially regulated and controlled."

During the year, the Commission was involved in numerous actions seeking injunctive and other relief against practices which it claimed to be unlawful under the securities laws.

The case of S.E.C. v. Texas Gulf Sulphur Co., whose institution was discussed in the last annual report, proceeded to trial during the year. Following the close of the fiscal year, the district court rendered a decision agreeing with certain of the contentions of the Commission both as to law and fact and disagreeing with others. It dismissed the Commission's complaint against Texas Gulf Sulphur Co. and 10 individual defendants but found that 2 other individual defendants committed violations of Section 10 (b) of the Securities Exchange Act of 1934 and Rule 10b-5 under that Act by purchasing Texas Gulf stock on the basis of material inside information. Texas Gulf began exploratory drilling near Timmins, Ontario, in November 1963. On April 16, 1964, it issued a press release announcing that it had made a major discovery of copper, zinc and silver. The Commission charged that officers, directors, and employees of Texas Gulf violated Section 10 (b) and Rule 10b-5 by purchasing Texas Gulf stock and calls during the intervening period on the basis of undisclosed inside information about the drilling results and by divulging this information to their relatives and friends so that these "tippees" could also purchase Texas Gulf securities on this basis. Some of the individual defendants were also charged with accepting stock options from the corporation during this period without disclosing the information in their possession about the drilling results to those making the decision to issue the options. Finally, the Commission charged the corporation with issuing a false and misleading press release 4 days before the press release announcing the discovery.

The court rejected defendants' contentions that the Commission must prove scienter, intent to deceive, reliance and causation in order to establish violations of Rule 10b-5 and that Section 16 of the 1934 Act is the only limitation on insider trading. It held that under Rule 10b-5 "an insider's liability for failure to disclose material information which he uses for his own advantage in the purchase of securities extends to purchases made on national securities exchanges as well as to purchases in 'face-to-face' transactions." The court further ruled that "insiders subject to the disclosure requirements of Section 10 (b) and Rule 10b-5 may include employees as well as officers, directors, and controlling stockholders who are in possession of material undisclosed information obtained in the course of their employment."

On the basis of these legal rulings the court found violations by the two individual defendants who purchased Texas Gulf securities on April 15, and April 16, 1964. It rejected their contentions that they were free to trade merely because rumors about the discovery were current in the press and financial circles, an article emanating from the corporation had appeared in a trade publication of limited circulation and an official of the Canadian government had issued a statement of undetermined circulation. It referred to the press release by the corporation as the "official announcement."

Contrary to the position urged by the Commission, the court held that other insiders who purchased stock and gave tips on April 16, 1964, did not commit violations, stating that insiders are free to trade on the basis of inside information once this information has been delivered to the news media, even though it has not appeared anywhere. The court also

decided that purchases of stock and calls and the giving of tips by insiders prior to April 9 did not violate Rule 10b-5 because the results of the mineral exploration did not constitute material facts at that time. The court agreed with the Commission that corporate officials responsible for the issuance of stock options are entitled to rely on the information furnished to them by management. It concluded that a member of the higher echelon of management who accepts a stock option without disclosing to the responsible officers all material information violates Section 10 (b) and Rule 1 Ob-5, but that employees who are not members of the higher echelon are entitled to assume that information already known to their superiors will be reported by them to the appropriate corporate officials.

In clearing the corporation of charges of violation the court ruled that a press release issued by a corporation is issued "in connection with the purchase or sale of any security" and, therefore, comes within Section 10 (b) and Rule 10b-5 only "if its purpose is to affect the market price of a company's stock to the advantage of the company or its insiders." It found no such purpose in this case. Alternatively, the court held that the accuracy of the press release must be judged only on the basis of information actually known to the drafters of the release at the time of its issuance, and that on the basis of such information the release in this case was not false or misleading. The Commission has appealed.

In S.E.C.. v. Georgia-Pacific Corporation the defendants consented to the entry of a decree enjoining them from violating Section 10 (b) of the Exchange Act and Rules 10b-5 and 10b-6 thereunder. Georgia-Pacific had entered into agreements to purchase the assets or stock of several corporations through the issuance of Georgia-Pacific stock. The agreements provided that the acquisition price would depend in part on the future price of Georgia-Pacific stock on the New York Stock Exchange during certain periods which were to be determined by Georgia-Pacific itself. The Commission's complaint alleged that certain officers and an employee of Georgia-Pacific had caused the employee pension funds to purchase Georgia-Pacific stock on the Exchange for the purpose of raising the price of the stock and resulting in the issuance of fewer shares by Georgia-Pacific. The consent decree set forth restrictions on future purchases of Georgia-Pacific stock by the company and its pension funds, including a prohibition on such purchases during any valuation period or within a 10-day period prior thereto.

In S.E.C.. v. Skagit Valley Telephone Co., et al., the Commission charged certain officials of the company with violations of the anti-fraud provisions of the securities acts in connection with the purchase and sale of the company's securities. The complaint alleged that these officials purchased shares from stockholders at prices of $5 and $10 per share without disclosing the true value of the stock and the offers that had been made for the stock, and thereafter sold such shares at $300 per share. The Commission also charged the company which purchased the stock at $300 from the officials and from other stockholders with violations of the anti-fraud provisions for conspiring with the other defendants to conceal the fact that others were willing to pay even more than $300 per

share. In addition to consenting to the issuance of decrees enjoining future violations, the defendants filed undertakings with the court as a result of which approximately $400,000 was deposited in a fund to be distributed to the defrauded stockholders.

In S.E.C.. v. VTR, Inc., et al., the Commission charged that a group of defendants controlling VTR had misappropriated company funds to finance their own personal investment ventures and had concealed their misappropriations through false annual reports and proxy statements. The Commission sought injunctive relief and the appointment of a receiver. The defendants consented to a permanent injunction requiring them to make an accounting and restitution for their unauthorized withdrawals and enjoining them from further violations of the reporting and anti-fraud provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934. In lieu of appointing a receiver, the court directed the controlling group to cause the election of four independent directors (of a five-man board) designated by the court to supervise the filing of proper annual reports and proxy statements with the Commission and to supervise a determination of the exact amount misappropriated. Pursuant to the consent judgment, the defendants were ordered to make restitution of more than $1.2 million. Restitution has been made of all but about $70,000, for which a note has been given.

A significant aspect of this case was the court's determination that jurisdiction under the Securities Act over a foreign business entity and a resident foreign national could be acquired by personal service of the summons and complaint in West Germany. This was the first opinion dealing with this question. The defendants had argued that such service was ineffective and that as foreign nationals they should not be subject to United States courts, since " 'physical power' is the sine qua non of jurisdiction." The court stated:

"Here there clearly was business transacted by the defendants in this state. Further, the SEC rules which protect both foreign and domestic investors who trade on our national exchanges could be evaded at will if injunctions could not be had against foreign based brokers and individuals who trade in large volume on such exchanges."

In S.E.C.. v. Seaboard Securities Corporation the court enjoined the defendant securities dealer and its president, Leon Nash, from charging their customers prices not reasonably related to the prevailing market prices with respect to any securities, not merely the two securities referred to in the complaint. In granting the Commission's request for a broad injunction, the court stated

"Having observed the defendant Nash, and having heard his insistence that the statutory and regulatory prohibitions are intolerable, we think it insufficient to enjoin repetitions of the forbidden actions only with respect to the two particular stocks in question . . . ."

In S.E.C.. v. S & P National Corporation, et al., the Commission alleged (1) that the corporate defendants have been unregistered investment companies for many years and have transacted business in violation of the Investment Company Act of 1940, (2) that

reports filed by S & P National Corporation pursuant to the requirements of the Securities Exchange Act of 1934 were false and misleading in failing to state that David M. Milton, one of the individual defendants, was a parent or director of S & P and in stating that certain persons, who had resigned or abandoned their offices, were directors of S & Pl* and (3) that the individual defendants had been derelict in permitting or causing the above violations. Upon motion of the Commission, preliminary injunctions were granted restraining the corporate defendants in the operation of their business as investment companies, and a receiver-trustee for the corporations was appointed.

In affirming the above orders, the Court of Appeals for the Second Circuit stated that although the Securities Exchange Act does not expressly provide for the appointment of a receiver or trustee, such an appointment may be made under that Act by virtue of the court's equitable powers, as well as under the Investment Company Act, which provides for the appointment of a trustee, to "bring the companies into compliance with the law, 'ascertain the true state of affairs . . . and report thereon' to the court and public shareholders and preserve the corporate assets." The court also held that if a company initially met and presently meets the assets test established by the Investment Company Act, then it has been, over the intervening years, an investment company subject to the Act even though it might not have met that test in every one of those years.

In S.E.C., v. Wong, the United States District Court for the District of Puerto Rico denied motions to dismiss by the defendants. The court rejected the argument that the change in the status of Puerto Rico (in 1952) from a territory of the United States to a Commonwealth deprived the court of jurisdiction over violations of the Federal securities laws. The court also ruled that under Section 36 of the Investment Company Act, providing for injunctive action for gross abuse of trust against "a person serving or acting" as an officer or director of a registered investment company, an action may be brought against a former officer or director who had resigned prior to institution of the action. The court stated that the quoted phrase referred to the defendant's capacity at the time the abuse of trust occurred. It further ruled that in an action under Section 36 or under Section 10 (b) of the Exchange Act, the Commission may seek as ancillary relief restitution and an accounting, since the prayer for injunctive relief invokes the full equitable powers of the court.

In S.E.C.. v. Tax Service, Inc. and John C. Bennett, the Court of Appeals for the Fourth Circuit affirmed a permanent injunction entered by the district court enjoining the defendants from offering or selling unregistered shares of Tax Service, Inc. The issuer is the publisher and distributor of "Tax Calculators" which contain a series of tables for the use of attorneys, accountants and others engaged in preparing income tax returns. The court held that the offer or sale of these securities, although limited to the issuer's subscribers and to the members of a local bar association, did not meet the requirements for a private offering exempt from registration under the Securities Act. It stated that neither an offeree's position as a subscriber nor the general acumen of attorneys in tax matters has any bearing on their access to the kind of information which registration

would make available and that "obviously, familiarity with the issuer's publications would not connote familiarity with the issuer's financial status." Decisions of the Commission dismissing applications for review of disciplinary action taken by the National Association of Securities Dealers, Inc. (NASD) were upheld in Merritt, Vickers, Inc. v. S.E.C. and Handley Investment Company v. S.E.C. In the Merritt, Vickers case, the NASD had found that the firm and its principals violated NASD rules by selling securities at prices not reasonably related to the current market; improperly extending credit; failing to maintain required books and records; and failing to disclose the firm's dual agency role and double commissions received. Rejecting the contention that the NASD improperly relied on the "pink sheets" in assessing the fairness of mark-ups, the court agreed with the Commission that "although the quotations in the sheets are not firm offers for a fixed number of securities, and final prices are subject to change, they constitute sufficient proof of prevailing market prices 'in the absence of evidence to the contrary'."

Petitioners urged that the Commission should have permitted them to adduce additional evidence bearing on the fairness of the mark-ups, claiming that they did not request production of such evidence in the hearings before the NASD because it would have been futile in view of the NASD's lack of subpoena power. The court found the argument "not persuasive," stating that "there is nothing in the record to demonstrate that process would have been required to obtain the desired information. Mere speculation cannot serve as an excuse for failure to produce relevant evidence before the NASD."

In the Handley case, the court rejected the argument that the NASD's disciplinary proceedings were akin to criminal proceedings and that violations had to be established by convincing evidence overcoming a presumption of innocence. The court indicated that the NASD and Commission should have wide latitude in establishing professional standards, stating,

"Absent constitutional or statutory infirmities, none of which appear here, the professional standards established by NASD and SEC for those engaging in over-the-counter securities business will not be upset by the courts. Petitioner failed to abide by those standards. The disciplinary action was not excessive, oppressive, or an abuse of discretion."

In M. G. Davis & Co., Inc. v. Cohen, the court granted the Commission's motion for summary judgment dismissing an action to enjoin the Commission from continuing a public proceeding instituted to determine whether the broker-dealer registration of the corporate plaintiff should be revoked and whether corresponding sanctions should be imposed against the individual plaintiffs. In considering the question of its jurisdiction to entertain an action for injunctive relief against the Commission prior to exhaustion of administrative remedies the court stated:

".. a District Court under its general federal question equity jurisdiction, 28 U.S.C. § 1331, is empowered to correct agency conduct 'in excess of its delegated powers and contrary to specific prohibition of the Act'. . . . The test to be applied in determining whether this 'narrow' exception to the customary avenues of review may be invoked . . . is 'whether the Commission has stepped plainly beyond the bounds of its statutory authority, or has acted in clear defiance of [plaintiffs'] constitutional rights to [their] irreparable damage'."

The opinion also provides an important interpretation of Section 15 (b) (7) of the Exchange Act, which was part, of the 1964 amendments to that Act. It held that the provisions of that Section, permitting censure, barring, or suspension of any person, may be applied with respect to statutory violations which occurred prior to the enactment of the provision. Plaintiffs had argued against such a "retroactive" application, but the court observed that "the amendment simply provides the Commission with a procedural device for accomplishing the same enforcement objectives which could formerly be achieved only circuitously," and ruled that "salesmen who have committed securities violations in the past could with justification be excluded or suspended from a profession demanding the utmost in probity from its members."

In Holmes v. Cary, the Court of Appeals for the Fifth Circuit affirmed per curiam a decision of the United States District Court for the Northern District of Georgia that the Commission need not accept for filing a purported registration statement under the Securities Act of 1933 which was "totally frivolous" and "obviously not a bona fide attempt to qualify to sell securities to the investing public."

Two cases challenging the validity of the Commission's action under its Rules Relating to Investigations were concluded this year. In Commercial Capital Corporation v. S.E.C., the Court of Appeals for the Seventh Circuit held that a denial by the Commission, pursuant to Rule 6 of those rules, of a witness' request to purchase copies of the transcript of his testimony in a private investigation did not deprive the witness of due process and that "the sale or the withholding of copies of the transcript was within the sound discretion" of the Commission. The court stated that the legislative history of the Administrative Procedure Act shows that Congress was aware that investigations of the Commission, like those of a grand jury, might be thwarted if witnesses were able to obtain copies of their investigative transcripts. Suspected violators, if in possession of such transcripts, would be able to tailor their own testimony to that given by other witnesses or take economic or other reprisals against those who were about to testify. Accordingly, the court found that Congress had given agencies authority to deny for good cause a witness' request for a transcript of his testimony in a nonpublic investigation. In the course of its opinion, the court also questioned whether Congress intended a direct court review of orders entered by the Commission in the course of a non-public investigation.

In S.E.C. v. Higashi, the Court of Appeals for the Ninth Circuit held that a district court could properly condition enforcement of a subpoena issued in a private Commission investigation upon the Commission's permitting a director of the corporation to be accompanied and represented by the attorney for the corporation, despite the fact that the sequestration provisions of Rule 7 (b) of the Commission's Rules Relating to Investigations had been invoked. While stating that "the reason for and purpose of the Commission's rule are clear and there can be no question as to its necessity and general propriety," the court held that in this case the interests of the director were "directly and prejudicially" affected by his not being able to use the corporation's attorney and, accordingly, that invocation of the sequestration rule exceeded the discretion of the Commission.

In a companion subpoena enforcement action, Jenks v. S.E.C., the court of appeals rejected the defense of harassment advanced by a witness who had been subpoenaed, where the harassment charged was not of the witness but of the subjects of the investigation.

The Commission has successfully defended its administrative investigatory subpoenas in court proceedings to quash them. In Fountaine v. S.E.C. and S.E.C.. v. Isbrandtsen, recalcitrant witnesses attempted to have such subpoenas declared to be of no effect. The decisions in these cases, based upon the Supreme Court's ruling in Reisman v. Caplin, make it clear that since a witness is not subject to penalties in advance of judicial enforcement proceedings, the subpoenas may not be challenged prior to such proceedings. The Commission therefore retains the right to decide whether or not court proceedings reviewing and enforcing its subpoena should be instituted.

The Commission participated as amicus curiae this year in several cases relating to the applicability of the "short-swing" recovery provisions of Section 16 (b) of the Securities Exchange Act of 1934 to transactions by insiders involving conversions of senior securities. In Heli-Coil Corp. v. Webster, described in the last Annual Report, convertible debentures were converted into common stock by an insider within 6 months after he had purchased the debentures. He then sold the common stock within 6 months after the conversion. The Court of Appeals for the Third Circuit, agreeing with the views expressed by the Commission as amicus curiae, held, in an en banc decision, that the conversion of the debentures into common stock constituted a sale of the debentures and a purchase of the common stock within the meaning of Section 16 (b), that the stock acquired upon conversion was not exempt from Section 16 (b) as a security "acquired in good faith in connection with a debt previously contracted," and that the conversion was not exempt from Section 16 (b) as an arbitrage transaction, but that no profit was realized from the disposition of the debentures upon conversion. Accordingly, the court held that recovery should be limited to the profits realized from the sale of the common stock.

In Blau v. Lamb, the Court of Appeals for the Second Circuit, disagreeing with the decision in Heli-Coil, held that a conversion of preferred stock into common was not a

sale of the preferred within the meaning of Section 16 (b). The court also held, inter alia, (1) that an acquisition of stock by a corporation wholly owned or controlled by an individual from another corporation 97-percent owned or controlled by him is not a purchase within the meaning of Section 16 (b) and (2) that when transactions which precede a stock dividend or stock split are to be matched against transactions which follow it, there must be a proportionate adjustment in the price of the shares involved in the earlier transactions in order to determine the true measure of the profit realized. The court's holdings on the latter two points were in accord with the views expressed by the Commission as amicus curiae. With respect to the conversion question, however, the Commission had urged that although, in its view, no profit was realized from the disposition of the preferred stock upon conversion, the conversion nevertheless constituted a sale of the preferred within the meaning of Section 16 (b).

In Blau v. Oppenheim the court adopted the view urged by the Commission as amicus curiae that a plaintiff who purchased shares in a corporation whose wholly-owned subsidiary had acquired all the assets and by merger succeeded to the business of the issuer in whose securities the short-swing trading occurred was entitled to sue under Section 16 (b) of the 1934 Act to recover the short-swing profits. The court held that there is "no support for the defendant's position that Congress intended that suits for the recovery of short-swing profits be restricted to the initial issuer whose securities were the subject of the illicit gains and its security holders, thus leaving no remedy in those instances where, as here, the issuer by a transfer of all its assets to another corporation has become extinct and is without its original security holders."

The case of S.E.C.. v. Golconda Mining Co. and Harry F. Magnuson had been instituted by the Commission in the Southern District of New York. The defendants moved to transfer the action to the District of Idaho, but the district court, agreeing with the contentions of the Commission, denied the motion. The court of appeals held that a petition for a writ of mandamus rather than for leave to appeal was the appropriate procedure for review of such an order but declined to grant the writ in this case since there had been "no clear-cut abuse of discretion."

CRIMINAL PROCEEDINGS

The statutes administered by the Commission provide that the Commission may transmit evidence of violations of any provisions of these statutes to the Attorney General, who in turn may institute criminal proceedings. Where an investigation by the Commission's staff indicates that criminal prosecution is warranted, a detailed report is prepared. After careful review by the General Counsel's Office, the report and the General Counsel's recommendations are considered by the Commission, and if the Commission believes criminal proceedings are warranted the case is referred to the Attorney General and to the appropriate U.S. Attorney. Commission employees familiar with the case generally assist the U.S. Attorney in the presentation of the facts to the grand jury, the preparation of

legal memoranda for use in the trial, the conduct of the trial, and the preparation of briefs on appeal.

During the past fiscal year 44 cases were referred to the Department of Justice for prosecution. As a result of these and prior referrals, 50 indictments were returned against 193 defendants and 76 defendants were convicted in 39 cases. Convictions of 17 defendants were affirmed in 11 cases and appeals were still pending in 9 other criminal cases at the close of the fiscal year. Of 10 defendants in 7 contempt cases pending during the year, 4 defendants were convicted and 5 cases involving 6 defendants were still pending.

As in prior years, the majority of criminal cases prosecuted involved the offer and sale of securities by fraudulent representations and other fraudulent practices. It is obviously not feasible to describe individually each of the many criminal matters pending or decided during the fiscal year; only a few of the more noteworthy ones can be singled out for discussion.

The conviction of Daniel E. Armel and others by a jury in the Southern District of Ohio culminated the Commission's investigation of the corporate "empire" of Armel. The fraudulent offer and sale of securities of the numerous corporations which made up the "empire" resulted in the loss of over 9 million dollars to investors. Two of the defendants convicted, Donald Hathaway and Jack Singleton, were certified public accountants who actively assisted Armel in perpetrating this fraud. Armel, the chief architect of the fraudulent promotion, received a sentence of 15 years imprisonment.

The Commission continued its enforcement of the registration requirements of Section 5 of the Securities Act of 1933 with the prosecution of criminal violations of these requirements not accompanied by charges of fraud. Herman Shaw and The Aquafilter Corporation, of which Shaw was president and controlling stockholder, were indicted in the Southern District of New York for violating Section 5 in the offer and sale of unregistered securities of Aquafilter. William F. Kane and Myron Freudberg were indicted in the same district for violating Section 5 in the offer and sale of unregistered securities of American Dryer Corporation. Shaw and Aquafilter pleaded guilty, and Shaw was sentenced to 30 days' imprisonment, fined $3,000 and placed on probation for 1 year, while the corporation was fined $12,500. Kane and Freudberg are awaiting trial.

The Commission's investigation of the sale of American Bonded Mortgage Company, Inc. securities culminated in the indictment of Mark H. Kroll, William Cahn and six other persons in the Southern District of Florida, for the fraudulent sale of various securities of this company and its affiliates. The indictment charged the defendants with devising and employing a fraudulent scheme to distribute notes purportedly "guaranteed" by mortgages on owner-occupied homes. This case is the latest in the Commission's continued effort to combat new variations of the old "Ponzi" scheme whereby investors are paid purported "interest" at very high rates with their investments "guaranteed" by

alleged valuable collateral. The so-called interest is in fact paid with funds obtained from other investors.

Near the close of the fiscal year, an indictment was returned by a Federal Grand Jury in Indianapolis charging 23 individuals and 6 corporations with defrauding investors in securities of Air and Space Underwriters, Inc. The indictment also charged The Indiana Investor and Business News, Inc. and its editor, Van C. Vollmer, with publishing and causing the publication of newspaper articles which, though not purporting to offer the securities of Air and Space Underwriters, Inc., described these securities for a consideration without disclosing the receipt of such consideration.

During the year the first criminal action for violations of Section 37 of the Investment Company Act of 1940 was prosecuted. The case is further discussed at p. 101, supra.

One of the more important appellate decisions rendered during the year was that of the Court of Appeals for the Second Circuit in United States v. Abrams. In affirming the convictions of Joseph Abrams and Sydney Albert for violating and conspiring to violate the registration provisions of the Securities Act in the distribution of their shares of Automatic Washer Company, the court found that there was more than sufficient evidence from which the jury could conclude that Abrams utilized nominee accounts as conduits for the subsequent distribution of these securities. The court also found that the evidence presented a question for the jury to determine whether Albert, in placing his Automatic stock with various banks as collateral for the repayment of loans, intended not to repay the loans and to have the stock distributed without registration. The affirmance of these convictions should serve as a warning to unscrupulous promoters that they cannot evade the registration requirements of the Securities Act by spurious reliance on exemptions from those requirements.

COMPLAINTS AND INVESTIGATIONS

Each of the Acts administered by the Commission specifically authorizes investigations to determine whether violations of the Federal securities laws have occurred.

The nine regional offices of the Commission, with the assistance of their respective branch offices, are chiefly responsible for the conduct of investigations. In addition, the Office of Enforcement of the Division of Trading and Markets of the Commission's headquarters office conducts investigations dealing with matters of particular interest or urgency, either independently or assisting the regional offices. The Office of Enforcement also exercises general supervision over and coordinates the investigative activities of the regional offices and recommends appropriate action to the Commission.

There are available to the Commission several sources of information concerning possible violations of the Federal securities laws. The primary source of information is

complaints by members of the general public concerning the activities of certain persons in securities transactions. The Commission's staff gives careful consideration to such complaints and, if it appears that violations may have occurred, an investigation is commenced. Other sources of information which are of assistance to the Commission in carrying out its enforcement responsibilities are the national securities exchanges, the National Association of Securities Dealers, Inc., brokerage firms, state and Canadian securities authorities, better business bureaus, and various law enforcement agencies.

It is the Commission's general policy to conduct its investigations on a confidential basis. Such a policy is necessary to effective law enforcement and to protect persons against whom unfounded or unconfirmed charges might be made. The Commission investigates many complaints where no violation is ultimately found to have occurred. To conduct such investigations publicly would ordinarily result in hardship or embarrassment to many interested persons and might affect the market for the securities in question, resulting in injury to investors with no countervailing public benefits. Moreover, members of the public would tend to be reluctant to furnish information concerning violations if they thought their personal affairs would be made public. Another advantage of confidential investigations is that persons suspected of violations are not made aware that their activities are under surveillance, since such awareness might result in frustration or obstruction of the investigation. Accordingly, the Commission does not generally divulge the result of a non-public investigation unless it is made a matter of public record in proceedings brought before the Commission or in the courts.

When it appears that a serious violation of the Federal securities laws has occurred or is occurring, a "case" is opened and a full investigation is conducted. Under certain circumstances it becomes necessary for the Commission to issue a formal order of investigation which appoints members of its staff as officers to issue subpoenas, to take testimony under oath and to require the production of documents. Usually this procedure is resorted to only when the subjects of the investigation and others involved are uncooperative and it becomes necessary to invoke the subpoena power to complete the investigation. During the fiscal year ended June 30, 1966, the Commission issued 136 such formal orders.

When an investigation has reached the stage at which enforcement action appears, appropriate, the Commission may proceed in one of several ways, although the use of one procedure may not necessarily preclude the use of another. The Commission may: (1) refer the case to the Department of Justice or appropriate local enforcement authorities for criminal prosecution, (2) institute through its own staff, in the appropriate U.S. district court, civil proceedings for injunctive relief to halt further violations of law, and, (3) institute administrative proceedings if the case is one where it has the power to do so.

The following table reflects in summarized form the investigative activities of the Commission during fiscal 1966:

[table omitted]

ENFORCEMENT PROBLEMS WITH RESPECT TO FOREIGN SECURITIES

In recent years the volume of unlawful Canadian promotions reaching into the United States has declined sharply from the 1950's when Montreal and Toronto "boiler-rooms" were conducting extensive high-pressure mail and telephone stock-selling campaigns into the United States. The decline is due primarily to the increased cooperation and liaison with the Commission by the Ontario and Quebec Securities Commissions and quasi-official regulatory bodies such as the Toronto Stock Exchange and the Broker-Dealers' Association of Ontario. In fiscal 1966 the unlawful offer and sale of Canadian securities in the United States remained at a low level.

As a result of an investigation of Windfall Oils and Mines Limited by an Ontario Royal Commission, in which this Commission assisted, several persons, including the promoters of Windfall, were charged with criminal violations. The Commission has also assisted the Ontario Royal Commission on Atlantic Acceptance Corporation Limited in its investigation into the circumstances surrounding the downfall in June 1965 of Atlantic Acceptance, a large Canadian finance company. A member of this Commission's staff has testified at public hearings of the Royal Commission. That commission was appointed in the wake of Atlantic's financial collapse, which has had substantial repercussions in both Canada and the United States and caused substantial losses to certain United States institutional investors. Criminal charges have already been brought in Ontario against several persons.

The Commission continued to be confronted by unlawful promotions from the Bahamas, particularly those involving unregistered time deposit certificates issued by so-called "banks" chartered there. Following the Commission's issuance of a public warning release and the obtaining of injunctive relief against a Bahamian bank, the Bahamas passed new banking legislation designed to prevent the issuance of unregistered securities by Bahamian banks, and to reduce sharply the number of bank charters available. As a result of such legislation, there has been a noticeable reduction in unlawful offers and sales of unregistered Bahamian bank securities in the United States.

In dealing with fraudulent promotions from the Bahamas, Jamaica, Brazil and elsewhere, the Commission is continuing to benefit from the new, simplified procedures for obtaining foreign postal fraud orders. The Post Office Department has cooperated fully with the Commission's program.

During the year the Commission maintained its Foreign Restricted List, consisting of foreign companies whose securities the Commission had reason to believe were being, or recently had been, distributed in the United States in violation of the registration requirements of the Securities Act of 1933. As of June 30, 1966, 73 companies were on

the list. Continuing the trend of recent years, it was necessary to add only 2 Canadian companies to the list during the year, while 53 others were deleted following compliance with established procedures. The names of 15 Bahamian companies, 1 Panamanian company and 1 company whose place of incorporation has not been ascertained were added to the list. The current list and supplements thereto are issued to and published by the press, and copies are mailed to all registered broker-dealers and are made available to the public.

As a practical matter, most United States broker-dealers refuse to execute transactions in securities on the restricted list.

As of September 30, 1966, the list contained the names of 49 Canadian and 16 Bahamian companies, 1 Panamanian company, and 2 companies whose place of incorporation has not been ascertained (representing the addition of 2 companies and the deletion of 7 others since the end of the fiscal year) as follows:

FOREIGN RESTRICTED LIST

Canadian issuers

Alaska Highway Beryllium Venture

Anuwon Uranium Mines, Ltd.

Associated Livestock Growers of Ontario

Autofab, Ltd.

Bayonne Mine, Ltd.

Bonwitha Mining Co., Ltd.

Canol Metal Mines, Ltd.

Canford Explorations, Ltd.

Consolidated Woodgreen Mines, Ltd.

Crusade Petroleum Corp., Ltd.

Dayjon Explorers, Ltd.

Devonshire Mining Co., Ltd.

Fairmont Prospecting Syndicate

The Fort Hope Grubstake Guardian Explorations, Ltd.

International Claim Brokers, Ltd.

Ironco Mining & Smelting Co., Ltd.

Jack Haynes Syndicate

Keele Industrial Developments, Ltd.

Kenilworth Mines, Ltd.

Kennament Development Corp., Ltd.

Ladysmith Explorations, Ltd.

Leader Mining Corp., Ltd.

Mack Lake Mining Corp., Ltd.

Maple Leaf Investing Corp., Ltd.

March Minerals, Ltd.

Merrican International Mines, Ltd.

Mid-National Developments, Ltd.

New Mallen Red Lake Mines, Ltd.

Norart Minerals Limited

Norbank Explorations, Ltd.

North West Pacific Developments, Ltd.

Nu-Gord Mines, Ltd.

Nu-World Uranium Mines, Ltd.

Outlook Explorations, Ltd.

Paracanusa Coffee Growers, Ltd.

St. Lawrence Industrial Development Corp.

Ste. Sophie Development Corp.

St. Stephen Nickel Mines, Ltd.

Sastex Oil & Gas, Ltd.

Sinclair Prospecting Syndicate Success Mines, Ltd.

Trans-Oceanic Hotels Corp., Ltd.

Turbenn Minerals, Ltd.

Tyndall Explorations, Ltd.

Victoria Algoma Mineral Co., Ltd.

Vimy Explorations, Ltd.

Western Allenbee Oil & Gas Co., Ltd.

Wingdam & Lightning Creek Mining Co., Ltd.

Bahamian issuers

Bankers International Investment Corporation

British Colonial Bank of Commerce (Bahamas) Ltd.

Commons Bank and Trust Company, Ltd.

Compressed Air Corporation, Ltd.

Essex Bank and Trust Company, Ltd.

First Bahamas Investment Trust

Investment Bankers of Bahamas, Ltd.

Investments and Trust Company, Ltd.

Jomur Trust Company, Ltd.

Long Island Bank of the Bahamas, Ltd.

Lords Bank and Trust Company, Ltd.

New Zealand Bank and Trust Company (Bahamas) Ltd.

now known as Marlboro Bank and Trust Company

Parliament Bank and Trust, Ltd.

The Bank of World Commerce, Ltd.

Transworld Investment Bank, Ltd.

Whitechapel Bank, Ltd.

Panamanian issuers

Victoria Oriente, Inc.

Issuers whose place of incorporation not ascertained

American International Mining

Darien Exploration Company, S.A.

SECTION OF SECURITIES VIOLATIONS

A Section of Securities Violations is maintained by the Commission as a part of its enforcement program to provide a further means of detecting and preventing fraud in securities transactions. The Section maintains files which provide a clearinghouse for other enforcement agencies for information concerning persons who have been •charged with or found in violation of various Federal and state securities statutes. Considerable information is also available concerning Canadian violators. The specialized information in these files is kept current through the cooperation of various governmental and nongovernmental agencies. At the end of the fiscal year, the files contained information concerning 73,511 persons and firms. Included in the data processed by the Section during the year was information received from several states and Canada respecting 106 criminal actions, 45 injunctive actions, 246 cease and desist type orders and 116 other administrative orders, such as denials, suspensions and revocations.

During the fiscal year, the Section received and disposed of 3,180 "securities violations" letters and dispatched 1,634 communications to cooperating agencies. It added to the Commission's files information respecting 5,431 persons or firms, including information on 2,028 persons or firms not previously identified.

APPLICATIONS FOR NONDISCLOSURE OF INFORMATION

The Commission is authorized under the various Acts administered by it to grant requests for nondisclosure of certain types of information which would otherwise be disclosed to the public in applications, reports or other documents filed pursuant to these statutes. Thus, under paragraph (30) of Schedule A of the Securities Act of 1933, disclosure of any portion of a material contract is not required if the Commission determines that such disclosure would impair the value of the contract and is not necessary for the protection of investors. Under Section 24 (a) of the Securities Exchange Act of 1934, trade secrets or processes need not be disclosed in any material filed with the Commission. Under Section 24 (b) of that Act, written objection to public disclosure of information contained in any material filed with the Commission may be made to the Commission which is then authorized to make public disclosure of such information only if in its judgment such disclosure is in the public interest. Similar provisions are contained in Section 22 of the Public Utility Holding Company Act of 1935 and in Section 45 of the Investment Company Act of 1940. These statutory provisions have been implemented by rules specifying the procedure to be followed by applicants for a determination that public disclosure is not necessary in a particular case.

The number of applications granted, denied or otherwise acted upon during the year are set forth in the following table:

[table omitted]

ACTIVITIES OF THE COMMISSION IN ACCOUNTING AND AUDITING

The several Acts administered by the Commission recognize the importance of dependable informative financial statements which disclose the financial status and earnings history of a corporation or other commercial entity. These statements, whether filed in compliance with the requirements under those statutes or included in other material available to stockholders or prospective investors, are indispensable to investors as a basis for investment decisions. The Congress, cognizant of the fact that such statements lend themselves readily to misleading inferences or even deception, whether or not intended, included express provisions in the various Acts with respect to financial information required to be disclosed. Thus, for example, the Securities Act requires the inclusion in the prospectus of balance sheets and profit and loss statements "in such form as the Commission shall prescribe" and authorizes the Commission to prescribe the

"items or details to be shown in the balance sheet and earnings statement, and the methods to be followed in the preparation of accounts . . ." Similar authority is contained in the Securities Exchange Act, and even more comprehensive power is embodied in the Investment Company Act and the Public Utility Holding Company Act.

Pursuant to the broad rulemaking power thus conferred with respect to the preparation and presentation of financial statements, the Commission has prescribed uniform systems of accounts for companies subject to the Holding Company Act; has adopted rules under the Securities Exchange Act governing accounting for and auditing of securities brokers and dealers; and has promulgated rules contained in a single comprehensive regulation, identified as Regulation S-X, which governs the form and content of financial statements filed in compliance with the several Acts. This regulation is supplemented by the Commission's Accounting Series Releases, of which 104 had been issued as of the end of the fiscal year. These releases were inaugurated in 1937 and were designed as a program for making public from time to time opinions on accounting principles for the purpose of contributing to the development of uniform standards and practice in major accounting questions. The rules and regulations thus established, except for the uniform systems of accounts which are regulatory reports, prescribe accounting principles to be followed only in certain limited areas. In the large area of financial reporting not covered by such rules, the Commission's principal means of protecting investors from inadequate financial reporting, fraudulent practices and overreaching by management is by requiring a certificate of an independent public accountant, based on an audit performed in accordance with generally accepted auditing standards, which expresses an opinion as to whether the financial statements are presented fairly in conformity with accounting principles and practices which are recognized as sound and which have attained general acceptance.

The Securities Act provides that the financial statements required to be made available to the public through filing with the Commission shall be certified by "an independent public or certified accountant." The other three statutes permit the Commission to require that such statements be accompanied by a certificate of an independent public accountant, and the Commission's rules require, with minor exceptions, that they be so certified. The value of certification by qualified accountants has been conceded for many years, but the requirement as to independence, long recognized and adhered to by some individual accountants, was for the first time authoritatively and explicitly introduced into law in 1933. Under the Commission's rules, an accountant who is qualified to practice in his own state is qualified to practice before the Commission unless he has entered into disqualifying relationships with a particular client, such as becoming a promoter, underwriter, voting trustee, director, officer, employee, or stockholder; has demonstrated incompetence or subservience to management; or has engaged in unethical or improper professional conduct.

The Commission endeavors to encourage and foster the independence of the accountant in his relationships with his client so that he may better be able to perform the service to

the public contemplated by the Congress in the various Acts administered by the Commission. Because of his special status and responsibility, the accountant has a unique opportunity to be a leader in raising standards of investor protection. The financial statements provide the key information both in the distribution and trading of securities. The work of the accountant in their preparation and publication is vital. Independent accountants lend authority to management's representations by their opinions as experts, and they operate as a check on management in assuring that the financial data are fairly presented in accordance with generally accepted accounting principles.

The Commission is vigilant in its efforts to assure itself that the audits which it requires are performed by independent accountants; that the information contained in the financial reports represents full and fair disclosure; and that appropriate auditing and accounting practices and standards have been followed in their preparation. In addition, it recognizes that changes and new developments in financial and economic conditions affect the operations and financial status of the several thousand commercial and industrial companies required to file statements with the Commission and that accounting and auditing procedures cannot remain static and continue to serve well a dynamic economy. The Commission's accounting staff, therefore, studies the changes and new developments for the purpose of establishing and maintaining appropriate accounting and auditing policies, procedures and practices for the protection of investors. The primary responsibility for this program rests with the Chief Accountant of the Commission, who has general supervision with respect to accounting and auditing policies and their application.

Progress in these activities requires continuing contact and consultation between the staff and outside accountants both individually and through such representative groups as, among others, the American Accounting Association, the American Institute of Certified Public Accountants, the American Petroleum Institute, the Financial Analysts Federation, the Financial Executives Institute, and the National Association of Railroad and Utilities Commissioners, as well as many Government agencies. Recognizing the importance of cooperation in the formulation of accounting principles and practices, adequate disclosure and auditing procedures which will best serve the interests of investors, the American Institute of Certified Public Accountants, the Financial Analysts Federation, 'and the Financial Executives Institute appoint committees which maintain liaison with the Commission's staff.

In recent years the Accounting Principles Board of the American Institute of Certified Public Accountants has performed a vital function in this area. The work of the Board is reflected in accounting research studies and opinions for the guidance of the profession. Drafts of these studies are referred to the Commission's accounting staff for review and comment prior to publication.

The many daily decisions to be made which require the attention of members of the Chief Accountant's staff include questions raised by the operating divisions of the Commission,

the regional offices, and the Commission itself. As a result of this day-to-day activity and the need to keep abreast of current accounting problems, the Chief Accountant's staff continually reexamines accounting and auditing principles and practices. From time to time members of the staff are called upon to assist in field investigations, to participate in hearings and to review Commission opinions insofar as they pertain to accounting matters.

Profiling and other conferences with officials of corporations, practicing accountants and others are also an important part of the work of the staff. Resolution of questions and problems in this manner saves registrants and their representatives both time and expense. The 1964 amendments to the securities acts have brought many heretofore "unregulated" companies into contact with the Commission. In many cases, the independent accountants certifying the financial statements of such companies have been a primary bridge between the companies and the Commission. These companies and the accountants have also been assisted by members of the Commission and of its staff who have lectured and participated in institutes and symposiums sponsored by various groups in different parts of the country where the 1964 amendments have been explained.

Many specific accounting and auditing problems are found in the examination of financial statements required to be filed with the Commission. Where examination reveals that the rules and regulations of the Commission have not been complied with or that applicable generally accepted accounting principles have not been adhered to, the examining division usually notifies the registrant by an informal letter of comment. These letters of comment and the correspondence or conferences that follow continue to be a most convenient and satisfactory method of effecting corrections and improvements in financial statements, both to registrants and to the Commission's staff. Where particularly difficult or novel questions arise which cannot be settled by the accounting staff of the divisions and by the Chief Accountant, they are referred to the Commission for consideration and decision.

The increasing use by many companies of installment sales and similar credit practices and the significance of the increasing amounts of the related deferred income taxes involved caused the Commission to state its opinion as to the proper reporting to be followed with respect to such deferred income taxes. The opinion states that where installment receivables are classified as current assets in accordance with the operating cycle practice, the related liabilities or credit items maturing or expiring in the time period of the operating cycle, including the deferred income taxes on installment sales, should be classified as current liabilities. Installment receivables not realizable within 1 year and the related deferred income taxes may be classified consistently as noncurrent items. In financial statements filed with the Commission for fiscal years ending on or after December 31, 1965, assets and liabilities entering into the operating cycle must be classified consistently as current or noncurrent items. In addition, appropriate disclosure of the classification followed and amounts involved should be made.

During the year a review was made of the accountants' certificates filed under paragraph (a) (5) of Rule 206 (4)-2 under the Investment Advisers Act of 1940, which requires that at least once a year an independent public accountant verify by actual examination all funds and securities of clients held by an investment adviser. This review showed that there was a wide variation in the scope of the examinations made and in the content of the accountants' certificates. Accordingly, the Commission issued an accounting series release describing the nature of the examination to be made and the content of the accountant's certificate.

Comments received with respect to the proposed revision of Form X-17A-5, the annual report of financial condition required to be filed by brokers and dealers pursuant to Section 17 of the Securities Exchange Act of 1934, were under review during the fiscal year.

On the basis of information obtained in a non-public investigation conducted during the fiscal year, the Commission had reason to believe that there may have been a lack of adherence to auditing standards by a certified public accountant in connection with the preparation and submission of certain material to the Commission. As a conclusion to the investigation the Commission issued an order accepting the accountant's resignation from practice before the Commission.

Shortly after the close of the fiscal year the Commission issued its order accepting the withdrawal from practice before the Commission of Homer E. Kerlin, a certified public accountant.54 Proceedings had been instituted pursuant to Rule 2 (e) of the Commission's Rules of Practice to determine whether Kerlin, an accounting firm of which he had been a partner, and the senior partner of such firm, had engaged in unethical or improper professional conduct in connection with the preparation and certification of financial statements of the Olen Company, Inc. and its successor, the Olen Division of H. L. Green Company, Inc., in 1958 and 1959. Subsequent to the institution of such proceedings, the partnership was dissolved and the senior partner died. The remaining respondent, Kerlin, without admitting the allegations against him, agreed that he would not appear or practice before the Commission in the future, with the understanding that the proceedings would be dismissed as to him and that the Commission might issue a statement with respect to its action. Concurrently with its order accepting Kerlin's withdrawal and dismissing the proceedings, the Commission released a report of the staff's investigation, on the basis of which the staff had concluded that the conduct of the accounting firm in its audit of the Olen accounts, books and records represented a complete abdication of the responsibilities of an independent public accountant.

INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT

Section 15 of the Bretton Woods Agreements Act, as amended, exempts from registration under both the Securities Act of 1933 and the Securities Exchange Act of 1934 securities

issued, or guaranteed as to both principal and interest, by the International Bank for Reconstruction and Development. The Bank is required to file with the Commission such annual and other reports with respect to such securities as the Commission determines to be appropriate in view of the special character of the Bank and its operations, and necessary in the public interest or for the protection of investors. The Commission has, pursuant to the above authority, adopted rules requiring the Bank to file quarterly reports and also to file copies of each annual report of the Bank to its board of governors. The Bank is also required to file reports with the Commission in advance of any distribution in the United States of its primary obligations. The Commission, acting in consultation with the National Advisory Council on International Monetary and Financial Problems, is authorized to suspend the exemption at any time as to any or all securities issued or guaranteed by the Bank during the period of such suspension.

The Bank reported a net income of $143.7 million for the fiscal year ending June 30, 1966. This compared with net earnings of $136.9 million in the fiscal year 1965.

On July 28, 1966, the Executive Directors allocated $67.8 million from the year's net income to the Supplemental Reserve against losses on loans and guarantees, increasing it to $731.6 million. This raised the Bank's total reserves, including the Special Reserve, to $1,021.4 million. The Executive Directors recommended to the Board of Governors that $75 million of the year's earnings be transferred to the Bank's affiliate, the International Development Association.

During the year, the Bank made 37 loans totaling $839.2 million, compared with a total of $1,023.3 million last year. The loans were made in Brazil, Chile, Colombia, Ethiopia, Finland, Guinea, Iran, Israel, Jamaica, Japan, Kenya, Tanzania and Uganda (East African Common Services Authority), Liberia, Malaysia, Mexico, Morocco, New Zealand, Nigeria, Pakistan, Paraguay, Peru, Philippines, Portugal, Spain, Sudan, Thailand, Tunisia and Venezuela. This brought the total number of loans to 461 in 79 countries and territories and raised the gross total of commitments to $9,793.8 million. By June 30, as a result of cancellations, exchange adjustments, repayments and sales of loans, the portion of loans signed still retained by the Bank had been reduced to $6,527.9 million.

During the year the Bank sold or agreed to sell $81.9 million principal amounts of loans, compared with sales of $106.2 million last year. As of the end of the fiscal year, the total of such sales was $1,966.6 of which all except $69 million had been made without the Bank's guarantee.

On June 30, 1966, the outstanding funded debt of the Bank was $2,805.9 million, reflecting a net increase of $81.9 million in the past year. During the year the funded debt was increased through the private placement of bonds and notes totaling the equivalent of $269.5 million, by the public sale in Canada of bonds totaling Can$ 20 million (US$18.5 million) and by the issuance of $17.9 million of bonds under delayed delivery arrangements. The debt was decreased through the retirement of bonds and notes totaling

the equivalent of $175.6 million, and by sinking and purchase fund transactions amounting to $48.4 million.

During the year Malawi and Zambia became members of the Bank, and Indonesia withdrew from membership. (On July 5, 1966, Indonesia applied for readmission.) The following 20 countries increased their capital subscriptions to the Bank by a combined total of $908.7 million: Austria, Ceylon, Finland, Germany, Guatemala, Iran, Iraq, Ireland, Israel, Jamaica, Japan, Jordan, Mexico, Norway, Saudi Arabia, South Africa, Spain, Sweden, Thailand and Uruguay. Thus on June 30, 1966, the subscribed capital of the Bank amounted to $22,426.4 million.

INTER-AMERICAN DEVELOPMENT BANK

The Inter-American Development Bank Act, which authorizes the United States to participate in the Inter-American Development Bank, provides 'an exemption for certain securities which may be issued by the Bank similar to that provided for securities of the International Bank for Reconstruction and Development. Acting pursuant to this authority, the Commission adopted Regulation IA, which requires the Bank to file with the Commission substantially the same information, documents and reports as are required from the International Bank for Reconstruction and Development. The Bank is also required to file a report with the Commission prior to the sale of any of its primary obligations to the public in the United States.

During the year ended June 30, 1966, the Bank made 14 loans totaling the equivalent of $97,750,000 from its ordinary capital resources, bringing the gross total of loan commitments outstanding to 129, aggregating $678,020,422. During the year, the Bank sold or agreed to sell $4,159,528 in participations in these loans. All participations were without the guarantee of the Bank except for a participation of $400,000 extended to one participant under a special agreement. The loans from the Bank's ordinary capital resources were made in Argentina, Brazil, Chile, Colombia, Costa Rica, Mexico, Nicaragua, Peru and Venezuela.

During the year the Bank also made 43 loans totaling the equivalent of $270,530,000 from its Fund for Special Operations, bringing the gross total of loan commitments outstanding to 99, aggregating $461,300,671. In addition, the Bank made 5 loans aggregating $18,800,000 from the Social Progress Trust Fund, which it administers under an Agreement with the United States, bringing the gross total of loan commitments outstanding to 117, aggregating $501,233,534.

On June 30, 1966, the outstanding funded debt of the ordinary capital resources of the Bank was the equivalent of $373,900,000, reflecting an increase during the year of the equivalent of $89 million. This increase consisted of two bond issues, including a $65 million short term issue of which $57 million was placed with the central banks or other

central financial institutions of 15 Latin American member countries and $8 million with central financial institutions of 2 non-member countries, Israel and Spain. The other bond issue consisted of Italian Lire in the amount of LIT 15,000,000,000 ($24,000,000). On June 27, 1966, the Bank entered into a loan agreement under which it is entitled to borrow the equivalent of $10 million in local currency from the Export-Import Bank of Japan. As of June 30, 1966, the Bank had not borrowed any Japanese Yen.

The subscribed ordinary capital of the Bank on June 30, 1966, was the equivalent of $1,769,820,000, of which $1,388,240,000 represented callable capital.

ASIAN DEVELOPMENT BANK

The Asian Development Bank Act, approved March 16, 1966, authorizes United States participation in a new Asian Development Bank and provides an exemption for certain securities which may be issued by the Bank similar to the exemptions afforded to the International Bank for Reconstruction and Development and the Inter-American Development Bank. As of the end of the fiscal year, the Asian Development Bank had not been formally organized.

STATISTICS AND SPECIAL STUDIES

The regular statistical activities of the Commission and its participation in the overall Government statistical program under the direction of the Office of Statistical Standards, Bureau of the Budget, have been continued in the Office of Policy Research. The statistical series described below are published in the Commission's monthly Statistical Bulletin. In addition, current figures and analyses of the data are published quarterly on new securities offerings, individuals' savings, stock trading of financial institutions, financial position of corporations, and plant and equipment expenditures.

Issues Registered Under the Securities Act of 1933

Monthly statistics are compiled on the number and volume of registered securities, classified by industry of issuer, type of security, and use of proceeds. Summary statistics for the years 1935-66 are given in Appendix Table 1 and detailed statistics for the fiscal year 1966 appear in Appendix Table 2.

New Securities Offerings

Monthly and quarterly data are compiled covering all new corporate and non-corporate issues offered for cash sale in the United States. The series includes not only issues publicly offered but also issues privately placed, as well as other issues exempt from registration under the Securities Act such as intrastate offerings and offerings of railroad

securities. The offerings series includes only securities actually offered for cash sale, and only issues offered for account of issuers.

Estimates of the net cash flow through securities transactions are prepared quarterly and are derived by deducting from the amount of estimated gross proceeds received by corporations through the sale of securities the amount of estimated gross payments by corporations to investors for securities retired. Data on gross issues, retirements and net change in securities outstanding are presented for all corporations and for the principal industry groups.

Individuals' Savings

The Commission compiles quarterly estimates of the volume and composition of individuals' savings in the United States. The series represents net increases in individuals' financial assets less net increases in debt. The study shows the aggregate amount of savings and the form in which they occurred, such as investment in securities, expansion of bank deposits, increases in insurance and pension reserves, etc. A reconciliation of the Commission's estimates with the personal savings estimates of the Department of Commerce, derived in connection with its national income series, is published annually by the Department of Commerce as well as in the Securities and Exchange Commission Statistical Bulletin.

Private Pension Funds

An annual survey is published of private pension plans other than those administered by insurance companies, showing the flow of money into these funds, the types of assets in which the funds are invested and the principal items of income and expenditures. Quarterly data on assets of these funds are published in the Statistical Bulletin.

Stock Trading of Financial Institutions

A new statistical report published in June 1966 contained data on stock trading of four principal types of financial institutions. Information on purchases and sales of common stock by private non-insured pension funds and non-life insurance companies has been collected on a quarterly basis by the Commission since 1964; these data are combined with similar statistics prepared for mutual funds by the Investment Company Institute and for life insurance companies by the Institute of Life Insurance. A quarterly release is being published in the current fiscal period.

Financial Position of Corporations

The series on the working capital position of all United States corporations, excluding banks, insurance companies and savings and loan associations, shows the principal

components of current assets and liabilities, and also contains an abbreviated analysis of the sources and uses of corporate funds.

The Commission, jointly with the Federal Trade Commission, compiles a quarterly financial report of all United States manufacturing concerns. This report gives complete balance sheet data and an abbreviated income account, data being classified by industry and size of company.

Plant and Equipment Expenditures

The Commission, together with the Department of Commerce, conducts quarterly and annual surveys of actual and anticipated plant and equipment expenditures of all United States business, exclusive of agriculture. After the close of each quarter, data are released on actual capital expenditures of that quarter and anticipated expenditures for the next two quarters. In addition, a survey is made at the beginning of each year of the plans for business expansion during that year.

Directory of Registered Companies

The Commission annually publishes a listing of companies required to file annual reports under the Securities Exchange Act of 1934. In addition to an alphabetical listing, there is a listing of companies by industry group classified according to The Standard Industrial Classification Manual.

Stock Market Data

The Commission regularly compiles statistics on the market value and volume of sales on registered and exempted securities exchanges, round-lot stock transactions on the New York exchanges for account of members and non-members, odd-lot stock transactions on the New York exchanges and block distributions of exchange stocks. Publication of odd-lot transactions in 75 selected stocks on the New York Stock Exchange was begun in the fall of 1964. Since January 1965, the Commission has also been compiling statistics on volume of over-the-counter trading in common stocks listed on national securities exchanges based on reports filed under Rule 17a-9 of the Securities Exchange Act dealing with the "third market."

Data on round-lot and odd-lot trading on the New York exchanges are released weekly. The other stock market data mentioned above, as well as these weekly series, are published regularly in the Commission's Statistical Bulletin.

OPINIONS OF THE COMMISSION

Formal administrative proceedings under the statutes administered by the Commission generally culminate in the issuance of an opinion and order. Where hearings are held, the hearing officer who presides normally makes an initial decision following the hearings, unless such decision is waived by the parties. Under an amended procedure which went into effect in April 1966, the initial decision includes an appropriate order. If Commission review is not sought, and if the case is not called up for review on the Commission's own initiative, the initial decision becomes the final decision of the Commission.

In those instances where it prepares its own decision, upon review or waiver of an initial decision, the Commission, or the individual Commissioner to whom a case may be assigned for the preparation of an opinion, is generally assisted by the Office of Opinions and Review. This Office is directly responsible to the Commission and is completely independent of the operating divisions of the Commission, consistent with the principle of separation of functions embodied in the Administrative Procedure Act. Where the parties to a proceeding waive their right to such separation, the operating division which participated in the proceeding may assist in the drafting of the Commission's decision.

The Commission's opinions are publicly released and are distributed to the press and to persons on the Commission's mailing list. In addition, they are printed and published periodically, by the Government Printing Office in bound volumes entitled "Securities and Exchange Commission Decisions and Reports."

Procedures for Publishing Hearing Examiners' Initial Decisions

The Commission recently adopted procedures to make the initial decisions of its hearing examiners more readily available to the public.

In accordance with the Commission's Rules of Practice, an announcement of the issuance of an initial decision in public administrative proceedings is carried in the Commission's News Digest. Copies of such decisions will be made available in the public reference room of the Commission's headquarters office, and in each regional and branch office. Those initial decisions which become the decisions of the Commission, and which the Commission determines are of precedential significance, will be published in whole or in part in the Securities and Exchange Commission Decisions and Reports.

In administrative proceedings which are conducted privately, the initial decision will not be made publicly available, unless the Commission otherwise orders, until the period within which review may be sought or ordered has expired and no review has been sought or ordered. Thereupon, except as noted below, the fact that the initial decision has been issued and become final will be announced by the Secretary, and copies will be made available and included in the Decisions and Reports as described above. Initial decisions in private proceedings which grant an application for confidential treatment or

conclude that the evidence does not sustain the violations charged will generally not be made public.

Only a limited supply of initial decisions is printed at the time of their issuance. Requests for copies will be honored until the supply is exhausted; thereafter, copies may be obtained only upon payment of the prevailing rate for reproductions.

DISSEMINATION OF INFORMATION

As the discussion in prior sections of this Report indicates, most large corporations in which there is a substantial public investor interest have filed registration statements or applications under the Securities Exchange Act or the Securities Act with the Commission and are required to file annual and other periodic reports. The financial and other data included in these documents receive widespread dissemination through the medium of securities manuals and other financial publications, thus becoming available to broker-dealer and investment adviser firms, trust departments and other financial institutions and through them, to public investors generally.

Various activities of the Commission facilitate public dissemination of corporate and other information. Among these is the issuance of a daily "News Digest" which contains (1) a resume of each proposal for the public offering of securities for which a Securities Act registration statement is filed; (2) a listing of those companies whose shares are traded over-the-counter which register with the Commission and of all companies which file interim reports reflecting significant corporate developments; (3) a summary of all orders, decisions, rules and rule proposals issued by the Commission; (4) a brief report of court actions resulting from the Commission's law enforcement program; and (5) a brief reference to each release issued by the Commission in its statistical studies. During the year, the News Digest reported information concerning among other things 1,697 registration statements filed under the Securities Act, 950 orders, decisions, rules and rule proposals, 272 court enforcement actions, and 74 statistical releases.

The News Digest is made immediately available to the press, and it is also reprinted and distributed by the Government Printing Office, on a subscription basis, to some 2,350 investors, securities firms, practicing lawyers and others. In addition, the Commission maintains mailing lists for the distribution of the full text of its orders, decisions, rules and rule proposals.

During the year, individual members of the Commission and numerous staff officers addressed various professional, business and other groups and participated in panel discussions of the laws administered by the Commission, the rules and regulations thereunder, and the policies, procedures and practices of the Commission. These speeches and discussions are helpful in promoting a better understanding of the functions and activities of the Commission, thus facilitating compliance with the laws and rules. In

addition, they stimulate public discussion of ways and means of improving the administrative process.

Information Available for Public Inspection

The many thousands of registration statements, applications, declarations and annual and other periodic reports filed with the Commission each year are available for public inspection at the Commission's principal office in Washington, D.C. In addition, copies of recent reports filed by companies having securities listed on exchanges other than the New York Stock Exchange and the American Stock Exchange, and copies of current reports of many non-listed companies, may be examined in the Commission's New York Regional Office. Recent reports filed by companies whose securities are listed on the New York and American Stock Exchanges may be examined in the Commission's Chicago Regional Office. Moreover, there are available for examination in all regional offices copies of prospectuses relating to recent public offerings of securities registered under the Securities Act; and all regional offices have copies of broker-dealer annual financial reports and Regulation A letters of notification filed in their respective regions.

Reports of companies whose securities are listed on the various exchanges may be seen at the respective exchange offices. In addition, the registration statements filed pursuant to the new Section 12 (g) of the Securities Exchange Act of 1934 are available for public inspection in the principal office in Washington, D.C., the New York, Chicago and San Francisco Regional Offices, and the regional office nearest the registrant.

In order to facilitate wider dissemination of financial and other information contained in corporate reports filed with the Commission under the Federal securities laws (an objective strongly urged by the Special Study Report), the Commission has arranged to take standing orders, on an experimental basis, for photocopies of annual reports filed on Form 10-K. This service may be extended later to other reports, depending upon public reception and the experience gained in supplying copies of annual reports.

Under the existing contract with a printing company for the reproduction of material in the Commission's public files in response to requests of members of the public, photocopies may be obtained at a cost of 10 cents per page for pages not exceeding 8 1/2" x 14" in size. The detailed per page prices are given in Release No. 34-7910, which may be obtained from the Publications Unit of the Commission. The charge for each certification of any document by the Commission is $2.

In order to make corporate reports more readily available for examination by interested members of the public, the Commission has also made arrangements for the Form 10-K annual reports and Form 10 registration statements to be placed on open shelves in the public area of its Public Reference Room in Washington, D.C., thus making these reports available for immediate inspection. There are presently three coin-operated photocopiers in the Public Reference Room to enable visitors to make immediate reproductions of

reports at a cost of 25 cents per page. (The New York Regional Office has a similar machine.)

Each year many thousands of requests for photocopies of and information from the public files of the Commission are received in the Public Reference Room in Washington, D.C. During the year 6,110 persons examined material on file in the Washington, D.C. office, and several thousand others examined files in the New York and Chicago regional offices. More than 15,400 searches were made for individuals requesting information and approximately 2,714 letters were written with respect to information required.

PUBLICATIONS

In addition to the daily News Digest, and releases concerning Commission action under the Acts administered by it and litigation involving securities violations, the Commission issues a number of other publications, including the following:

Weekly:

Weekly Trading Data on New York Exchanges: Round-lot and odd-lot transactions effected on the New York and American Stock Exchanges (information is also included in the Statistical Bulletin).

Monthly:

Statistical Bulletin.

Official Summary of Securities Transactions and Holdings of Officers, Directors and Principal Stockholders.

Quarterly:

Financial Report, U.S. Manufacturing Corporations (jointly with the Federal Trade Commission.) (Statistical Series Release summarizing this report is available from the Publications Unit.)

Plant and Equipment Expenditures of U.S. Corporations (jointly with the Department of Commerce).

New Securities Offerings.

Volume and Composition of Individuals' Saving.

Working Capital of U.S. Corporations.

Stock Transactions of Financial Institutions.

Annually:

Annual Report of the Commission.

Securities Traded on Exchanges under the Securities Exchange Act of 1934.

List of Companies Registered under the Investment Company Act of 1940.

Classification, Assets and Location of Registered Investment Companies under the Investment Company Act of 1940.

Private Noninsured Pension Funds (assets available quarterly in the Statistical Bulletin).

Directory of Companies Filing Annual Reports.

Other Publications:

Decisions and Reports of the Commission.

Judicial Decisions.

A Study of Mutual Funds (by The Wharton School).

Report of Special Study of Securities Markets.

Accounting Series Releases -- Compilation of 1-89.

Securities and Exchange Commission -- The Work of the Securities and Exchange Commission.

Commission Report on Public Policy Implications of Investment Company Growths

ORGANIZATION

During fiscal year 1966 and shortly thereafter, certain organizational changes were effected in accordance with the Commission's policy of continuing review of its organization and functional alignments.

In April 1966, the staff and functions of the Branch of Market Analysis of the Division of Trading and Markets were transferred to the Office of Policy Research, to be

consolidated with the Commission's economic and statistical studies and the compilation of data on program activities. At the same time, the staff and functions of the Chief Counsel's Office in the Office of Policy Research were transferred to the Office of Regulation in the Division of Trading and Markets, to assist directly in that Division's responsibilities for the regulation of the securities market. In addition, two Associate Directors were appointed for the Division of Trading and Markets, one to be responsible for Markets and Regulation, and the other for Enforcement.

In July 1966, a number of organizational changes were effected in the Division of Trading and Markets. The Office of Criminal Reference and the Office of Proceedings, which performed similar functions, were consolidated; the Branch of Distribution and Stabilization was abolished; and the three Branches of Enforcement were consolidated into two Branches.

PERSONNEL AND FINANCIAL MANAGEMENT

Highlights of the Commission's personnel management program in fiscal 1966 included (1) revision of its Conduct Regulation, (2) the granting of SEC "Distinguished Service" awards for outstanding career service, (3) participation with other regulatory agencies in a joint seminar program for summer students, and (4) the addition of an important fringe benefit in the form of income protection insurance.

Under Executive Order 11222 of May 8, 1965, "Prescribing Standards of Ethical Conduct for Government Officers and Employees," the Civil Service Commission issued broad regulations which established a uniform pattern for agency regulations and minimum requirements to be met. The Commission's Conduct Regulation, first adopted in 1953, "to restate the ethical principles which it believes should govern and have governed the conduct of Members and employees and former Members and former employees of the Securities and Exchange Commission," was accordingly revised as of March 21, 1966. The revised version clarified certain provisions of existing rules and added new rules required by the basic regulations of the Civil Service Commission, including rules relating to the disclosure by employees of information relating to their finances.

As part of its Eleventh Annual Service and Merit Awards Ceremony held in October 1965, the Commission inaugurated a new series of "Distinguished Service" awards for outstanding career service. The first four recipients of the awards -- Commissioner Byron D. Woodside; Robert H. Bagley, Associate Director, Division of Corporation Finance; Orval L. DuBois, Secretary of the Commission; and William Green, Administrator of the Atlanta Regional Office -- had a combined total of 124 years of SEC service.

The Commission and seven other regulatory agencies supplemented the 1965 White House Seminar Program for summer students by conducting a joint program entitled "Regulation in a Democracy." This half-day program, which included prepared

statements by the panel members and a question and answer session, was devoted to three topics:

"The Purpose of Regulation in a Democracy"

"The Tasks of Regulatory Agencies"

"Effects of Regulation on Our Daily Lives"

Almost 100 students attended, including 17 employed by the Commission.

In January 1966, under the sponsorship of the SEC Recreation and Welfare Association, all Commission employees were offered low-cost income protection insurance designed to minimize the financial burden in cases of illness or disability. The insurance, offered as an employee service at no cost to the Commission, is part of a continuing effort to make special-type insurance available to employees at low-cost group rates.

During the fiscal year 1966, within-grade salary increases in recognition of high quality work performance were granted to 54 employees. These awards are authorized by Section 702 of the Classification Act of 1949, as amended by the Salary Reform Act of 1962. In addition, cash awards totaling $3,500 were presented to 19 employees for superior performance and 6 employees received a total of $100 for adopted suggestions.

The following comparative table shows the personnel strength of the Commission as of June 30, 1965 and 1966:

[table omitted]

The table on page 151 shows, for the fiscal years 1962 to 1967, the status of the Commission's budget estimates from the initial submission to the Bureau of the Budget to final enactment of the annual appropriation.

The Commission is required by law to collect fees for or from (1) the registration of securities proposed to be offered; (2) qualification of trust indentures; (3) registration of exchanges; (4) brokers and dealers who are registered with the Commission but who are not members of a registered national securities association (the National Association of Securities Dealers (NASD) is the only such organization); and (5) certification of documents filed with the Commission. [Footnote: Principal rates are (1) 1/50 of 1 percent of the maximum aggregate price of securities proposed to be offered, or 20 cents per $1,000, with a minimum fee of $100 (Public Law 89-289, approved October 22, 1965, effective January 1, 1966); (2) 1/500 of 1 percent of the aggregate dollar amount of securities sales on the exchanges; (3) for fiscal 1965 : a basic registration fee of $100 for each non-NASD broker-dealer, plus $2 per associated person up to a limit of 100 persons, plus $1 for each additional associated person. For fiscal 1966: a base fee of $150 for each

non-NASD broker-dealer, plus $7 for each associated person, plus $30 for each office and $25 for each associated person joining such broker-dealer after August 1, 1966.]

The following table shows the Commission's appropriation, total fees collected, percentage of fees collected to total appropriation, and the net cost to the taxpayers of Commission operations for the fiscal years 1964, 1965 and 1966.
[table omitted]