Investment Bankers Conference, Inc.

1010 Vermont Avenue
Washington, D. C.

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WALLACE H. FULTON, *Director* FRANK L. SCHEFFEY, *Co-Director, New York*

January 18, 1938.

TO ALL MEMBERS OF THE CONFERENCE:

We are enclosing herewith a mimeographed copy of Senate Bill 3255 which was introduced in the Senate yesterday by Senator Francis T. Maloney of Connecticut, the purpose of which is:

> "To provide for the establishment of a mechanism of regulation among over-the-counter brokers and dealers operating in interstate and foreign commerce or through the mails comparable to that provided for national securities exchanges under the Securities Exchange Act of 1934."

If you have been following the work of the Conference over the past three years, and the thinking of leaders in the business and of officials of the Securities and Exchange Commission with respect to regulation of over-the-counter markets, you will realize at once the significance of this proposed legislation.

The Conference, from the very outset, has sponsored the principle of self-regulation as the most effective practical solution to the problem, and has worked diligently toward that end, although it has always been realized that completely effective self-regulation would be difficult, if not impossible, of achievement without express legal sanctions or recognition.

Mr. William O. Douglas, Chairman of the Securities and Exchange Commission, made it quite clear in his address before the Bond Club of Hartford on January 7, 1938 (the full text of which is contained in your CONFERENCE NEWS of January 8) that the problem of bringing about effective regulation of over-the-counter markets is second only on the Commission's agenda of market problems to that of securing effective regulation of the exchanges of the country. In that address the Chairman first discussed the possibility of more pervasive direct Federal regulation of over-the-counter markets; but as a much-to-be-preferred alternative to stricter direct Federal regulation he expressed the hope that the over-the-counter brokers and dealers of the country would themselves solve this problem through effective self-government, subject to supervision by the Commission.

Senator Maloney, who is much interested in over-the-counter market problems, has held conferences with representatives of the Commission and the industry as to the best means of securing effective regulation of such markets. The enclosed bill represents the Senator's present thought on this subject, but it is our understanding that he is desirous of having it thoroughly and critically examined by all interested parties and that he will welcome comments, suggestions and criticisms addressed to its improvement.

The Conference has been interested in the whole question of regulation for a long period of time, but neither the Governing Committee, nor any officer, nor any other committee of the Conference has taken any formal position or action on the enclosed bill. It will be the subject, however, of detailed discussion by the Governing Committee and Advisory Council at their meeting in New York on Monday, January 24, 1938; and later it will undoubtedly be studied by appropriate special committees of the Conference. It is likely, however, that the Conference will want to take a position on this bill as soon as possible, so you are earnestly requested to examine the bill and Mr. Douglas' speech at your earliest opportunity and to forward to this office promptly, if possible before January 24, any comments or criticisms which you may care to make thereon.

Very truly yours,

WALLACE H. FULTON,
Director.

Investment Bankers Conference, Inc.
1010 Vermont Ave., N. W.
Washington, D. C.

Copy of S. 3255, introduced January 17, 1938 by Senator Maloney

A BILL

To provide for the establishment of a mechanism of regulation among over-the-counter brokers and dealers operating in interstate and foreign commerce or through the mails, comparable to that provided by national securities exchanges under the Securities Exchange Act of 1934, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the Securities Exchange Act of 1934, as amended, is amended by inserting after section 15 thereof the following new section:

"Sec. 15A. (a) Any association of brokers or dealers may be registered with the Commission as a national securities association pursuant to subsection (b), or as an affiliated securities association pursuant to subsection (d), under the terms and conditions hereinafter provided in this section, by filing with the Commission a registration statement in such form as the Commission may prescribe, setting forth the information, and accompanied by the documents below specified:

"(1) Such data as to its organization, membership, and rules of procedure, and such other information as the Commission may by rules and regulations require as necessary or appropriate in the public interest or for the protection of investors; and

"(2) Copies of its constitution, charter, or articles of incorporation or association, with all amendments thereto, and of its existing bylaws, or of any rules or instruments corresponding to the foregoing, whatever the name, hereinafter in this title collectively referred to as the 'rules of the association'.

Such registration shall not be construed as a waiver of any constitutional right or of any right to contest the validity of any rule or regulation of the Commission under this title.

"(b) An applicant association shall not be registered as a national securities association unless it appears to the Commission that --

"(1) by reason of the number of its members, the scope of their transactions, and the geographical distribution of its members such association will be able to comply with the provisions of this title and the rules and regulations thereunder and to carry out the purposes of this section;

"(2) such association is so organized and is of such a character as to be able to comply with the provisions of this title and the rules and regulations thereunder, and to carry out the purposes of this section;

"(3) the rules of the association provide that any broker or dealer who makes use of the mails or of any means or instrumentality of interstate commerce to effect any transaction in, or to induce the purchase or sale of, any security otherwise than on a national securities exchange,

may become a member of such association, except such as are excluded pursuant to paragraph (4) of this subsection: Provided, That the rules of the association may restrict membership in such association on such specified geographical basis, or on such specified basis relating to the type of business done by its members, or on such other specified and appropriate basis, as appears to the Commission to be necessary or appropriate in the public interest or for the protection of investors and to carry out the purpose of this section;

"(4) the rules of the association provide, that except with the approval or at the direction of the Commission in cases in which the Commission finds it appropriate in the public interest so to approve or direct, no broker or dealer shall be admitted to or continued in membership in such association, if (1) such broker or dealer, whether prior or subsequent to becoming such, or (2) any partner, officer, director, or branch manager of such broker or dealer (or any person occupying a similar status or performing similar functions), or any person directly or indirectly controlling or controlled by such broker or dealer, whether prior or subsequent to becoming such, (A) has been and is suspended or expelled from a registered securities association (whether national or affiliated) or from a national securities exchange, for violation of any rule of such association or exchange which prohibits any act or transaction constituting conduct inconsistent with just and equitable principles of trade, or requires any act the ommission of which constitutes conduct inconsistent with just and equitable principles of trade, or (B) is subject to an order of the Commission denying or revoking his registration pursuant to section 15 of this title, or expelling or suspending him from membership in a registered securities association or a national securities exchange, or (C) is permanently or temporarily enjoined by order, judgment, or decree of any court of competent jurisdiction from engaging in or continuing any conduct or practice in connection with the purchase or sale of any security;

"(5) the rules of the association assure a fair representation of the membership in the adoption of any rule of the association or amendment thereto, the selection of its officers and directors, and in all other phases of the administration of its affairs;

"(6) the rules of the association provide for the equitable allocation of dues among the membership, to defray reasonable expenses of administration;

"(7) the rules of the association are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors, and to remove impediments to and perfect the mechanism of a free and open market; and are not designed to require or permit unfair discrimination between customers, or issuers, or brokers or dealers, nor to fix minimum profits or minimum rates of commission or other charges;

"(8) the rules of the association provide that members shall be appropriately disciplined, by expulsion, suspension, fine, censure or any other fitting penalty, for any violation of its rules;

"(9) the rules of the association provide a fair and orderly procedure with respect to the disciplining of members and the denial of membership to any broker or dealer seeking membership therein. In any proceeding to determine whether any member shall be disciplined, such rules shall require that specific charges be brought; that such member shall be notified of, and be given an opportunity to defend against, such charges; that a record shall be kept; and that the determination shall include

(A) a statement setting forth any act or practice in which such member may be found to have engaged, or which such member may be found to have omitted, (B) a statement setting forth the specific rule or rules of the association of which any such act or practice, or omission to act, is deemed to be in violation, (C) a statement whether the acts or practices prohibited by such rule or rules, or the omission of an act required thereby, are deemed to constitute conduct inconsistent with just and equitable principles of trade, and (D) a statement setting forth the penalty imposed. In any proceeding to determine whether a broker or dealer shall be denied membership, such rules shall provide that the broker or dealer shall be notified of, and be given an opportunity to be heard upon, the specific grounds for denial which are under consideration; that a record shall be kept; and that the determination shall set forth the specific grounds upon which the denial is based; and

"(10) the requirements of subsection (c) insofar as these may be applicable, are satisfied.

"(c) The Commission may permit or require the rules of an association applying for registration pursuant to subsection (b), to provide for the admission of an association registered as an affiliated securities association pursuant to subsection (d), to participation in said applicant association as an affiliate thereof, under terms permitting such powers and responsibilities to such affiliate, and under such other appropriate terms and conditions, as may be provided by the rules of said applicant association, if such rules appear to the Commission to be necessary or appropriate in the public interest or for the protection of investors and to carry out the purposes of this section. The duties and powers of the Commission with respect to any national securities association or any affiliated securities association shall in no way be limited by reason of any such affiliation.

"(d) An applicant association shall not be registered as an affiliated securities association unless it appears to the Commission that --

"(1) such association, notwithstanding that it does not satisfy the requirements set forth in paragraph (1) of subsection (b), will, forthwith upon the registration thereof, be admitted to affiliation with an association registered as a national securities association pursuant to said subsection (b), in the manner and under the terms and conditions provided by the rules of said national securities association in accordance with subsection (c); and

"(2) such association and its rules satisfy the requirements set forth in paragraphs (2) to (9), inclusive, of subsection (b); except that in the case of any such association any restrictions upon membership therein of the type authorized by paragraph (3) of subsection (b) shall not be less stringent than in the case of the national securities association with which such association is to be affiliated.

"(e) Upon the filing of an application for registration pursuant to subsection (b) or subsection (d), the Commission shall by order grant such registration if the requirements of this section are met. If, after appropriate notice and opportunity for hearing, it appears to the Commission that any requirement of this section is not satisfied, the Commission shall by order deny such registration. If any association granted registration as an affiliated securities association pursuant to subsection (d) shall fail to be admitted promptly thereafter to affiliation with a registered national securities association, the Commission shall revoke the registration of such affiliated securities association.

"(f) A registered securities association (whether national or affiliated) may, upon such reasonable notice and upon such terms and conditions relating to orderly liquidation as the Commission may deem necessary in the public interest or for the protection of investors, withdraw from registration by filing with the Commission a written notice of withdrawal in such form as the Commission may by rules and regulations prescribe. Upon the withdrawal of a national securities association from registration, the registration of any association affiliated therewith shall automatically terminate.

"(g) If any registered securities association (whether national or affiliated) shall take any disciplinary action against any member thereof, or shall deny admission to any broker or dealer seeking membership therein, such action shall be subject to review by the Commission, on its own motion, or upon application by any person aggrieved thereby filed within sixty days after such action has been taken or within such longer period as the Commission may determine. Application to the Commission for review, or the institution of review by the Commission on its own motion, shall not operate as a stay of such action, unless the Commission shall so order.

"(h) (1) In a proceeding to review disciplinary action taken by a registered securities association against a member thereof, if the Commission, after appropriate notice and opportunity for hearing, upon consideration of the record before the association and such other evidence as it may deem relevant, shall (A) find that such member has engaged in such acts or practices, or has omitted such act, as the association has found him to have engaged in or omitted, and (B) shall determine that such acts or practices, or omission to act, are in violation of such rules of the association as have been designated in the determination of the association, the Commission shall by order dismiss the proceeding, unless it appears to the Commission that such action should be modified in accordance with paragraph (2) of this subsection. The Commission shall likewise determine whether the acts or practices prohibited, or the omission of any act required, by any such rule constitute conduct inconsistent with just and equitable principles of trade, and shall so declare. If it appears to the Commission that the evidence does not warrant the finding required in clause (A), or if the Commission shall determine that such acts or practices as are found to have been engaged in are not prohibited by the designated rule or rules of the association, or that such act as is found to have been omitted is not required by such rule or rules, the Commission shall by order set aside the actions of the association.

"(2) If, after appropriate notice and opportunity for hearing, the Commission finds that any penalty imposed upon a member is excessive or oppressive, having due regard to the public interest and the established practice of such association and of other registered securities associations with respect to penalties, the Commission shall by order cancel, reduce, or require the remission of such penalty.

"(3) In any proceeding to review the denial of membership in a registered securities association, if the Commission, after appropriate notice and hearing, and upon consideration of the record before the association and such other evidence as it may deem relevant, shall determine that the specific grounds on which such denial is based exist in fact and are valid under this section, the Commission shall by order dismiss the proceeding; otherwise, the Commission shall by order set aside the action of the association and require it to admit the applicant broker or dealer to membership therein.

"(i) (1) The rules of a registered securities association may provide that no member thereof shall deal with any non-member broker or dealer (as defined in paragraph (2) of this subsection) except at the same prices, for the same commissions or fees, and on the same terms and conditions as are by such member accorded to the general public.

"(2) For the purposes of this subsection, the term 'non-member broker or dealer' shall include any broker or dealer who makes use of the mails or of any means or instrumentality of interstate commerce to effect any transaction in, or to induce the purchase or sale of, any security otherwise than on a national securities exchange, who is not a member of any registered securities association, except a broker or dealer who deals exclusively in commercial paper, bankers' acceptances, or commercial bills.

"(3) Nothing in this subsection shall be so construed or applied as to prevent any member of a registered securities association from granting to any other member of any registered securities association any dealer's discount, allowance, commission, or special terms.

"(j) Every registered securities association shall file with the Commission in accordance with such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors, copies of any changes in or additions to the rules of the association, and such other information and documents as the Commission may require to keep current or to supplement the registration statement and documents filed pursuant to subsection (a). No change in or addition to the rules of a registered securities association shall take effect until thirty days after the filing of a copy thereof with the Commission, or until such earlier date as the Commission may determine.

"(k) (1) The Commission is authorized by order to abrogate any rule of a registered securities association, or to prevent any rule from taking effect, if after appropriate notice and opportunity for hearing, it appears to the Commission that such abrogation or prevention is necessary or appropriate to assure fair dealing by the members of such association, to assure a fair representation of the membership in the administration of its affairs, or otherwise to protect investors or effectuate the purposes of this section.

"(2) The Commission may in writing request any registered securities association to adopt any specified alteration of or supplement to its rules with respect to any of the matters hereinafter enumerated. If such association fails to adopt such alteration or supplement within a reasonable time, the Commission is authorized by order to alter or supplement the rules of such association in the manner theretofore requested if, after appropriate notice and opportunity for hearing, it appears to the Commission that such alteration or supplement is necessary or appropriate in the public interest or for the protection of investors or to effectuate the purposes of this section, with respect to: (1) The basis for, and procedure in connection with, the denial of membership or the disciplining of members; (2) the method for adoption of any change in or addition to the rules of the association; (3) the method of choosing officers and directors; (4) affiliation between registered securities associations; (5) the prevention of fictitious quotations; (6) the prevention of fraudulent or manipulative acts or practices; (7) safeguards against unreasonable profits or unreasonable rates of commissions or other charges: Provided, That nothing herein shall authorize the imposition of any schedule of minimum or maximum prices, discounts, commissions, allowances or other charges; (8) safeguards against unfair discrimination between customers, or issuers, or brokers or dealers; (9) safeguards with respect to the financial responsibility of members and against the evasion of financial responsibility through the use of corporate forms, special partnerships or other devices; (10) the manner, method

of making settlements, payments or deliveries; (12) the collection, recording and dissemination of information relating to the over-the-counter markets; and (13) similar matters.

"(l) The Commission is authorized, if such action appears to it to be necessary or appropriate in the public interest or for the protection of investors and to carry out the purposes of this section --

"(1) after appropriate notice and opportunity for hearing, by order to suspend for a period not exceeding twelve months or to revoke the registration of a registered securities association, if the Commission finds that such association has violated any provision of this title or the rules and regulations thereunder, or has failed to enforce compliance with its own rules, or has engaged in any other activity inconsistent with the purposes of this section;

"(2) after appropriate notice and opportunity for hearing, by order to suspend for a period not exceeding twelve months or to expel from a registered securities association any member thereof who the Commission finds has violated any provision of the Securities Act of 1933 or of this title or the rules and regulations thereunder, or has effected any transaction for any other person who, he had reason to believe, was violating in respect of such transaction any provision of the Securities Act of 1933 or of this title or the rules and regulations thereunder;

"(3) after appropriate notice and opportunity for hearing, by order to remove from office any officer or director of a registered securities association who, the Commission finds, has failed to enforce the rules of the association, or has abused his authority.

"(m) If any provision of this section is in conflict with any provision of any law of the United States in force on the date this section takes effect, the provision of this section shall prevail."