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THE CONSTITUTION OF THE NEW YORK STOCK EXCHANGE

(AS REVISED IN 1925)

*An address before the
New York Stock Exchange Institute*

By H. S. MARTIN
First Assistant Secretary

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The subject assigned to me is: "The Constitution of the New York Stock Exchange, as revised in 1925." The possibilities comprised within the subject may be partially understood when it is remembered that the Special Committee which brought about the revision was occupied for something over three years with consideration of the subject; and it is too much to hope for more than a surface consideration in the few minutes allotted at this time.

First of all, What is a Constitution? The Century Dictionary and Encyclopedia gives the following definition:

"A system of fundamental principles, maxims, laws or rules embodied in written documents or established by prescriptive usage, for the government of a nation, state, society, corporation or association: as, the Constitution of the United States, the British Constitution, the Constitution of the State of New York; the constitution of a social club," etc.

It is possible that something of value may be obtained by consideration for a few moments, of the definition; we note that the British Constitution is given as an example—but, on examination, we are not able to get before us a copy of such a document; as a matter of fact, no such document or set of "principles, maxims, laws or rules" exists, at least not in the shape in which one may find the American Constitution, or that of New York. The British Constitution, so-called, comes within the

language of the definition "established by prescriptive usage," having been the growth of something over 700 years of gradual attainment by the British nation, since the day when Magna Charta was forced from the hands of an unwilling King, from which sturdy root has grown the present freedom of all English-speaking races, through the upspringing of other roots or branches forced from some other unwilling King or equally unwilling House of Lords or other power.

All Constitutions have been instituted only by the consent of the governed, and can be altered by that consent. The Constitution of this country was so established, and has been so altered. Whenever an act of a Legislature or of a Congress is declared by the Courts to be unconstitutional, it would be ludicrous if it were not pitiful to listen to assaults made upon such decision; for it must be apparent that the people consented first to the Constitution, then to the power of Courts to construe that Constitution; and finally that the people have the power to so amend the Constitution that the principle objected to as unconstitutional can be made constitutional. We need here to give but a single instance of such a change in our fundamental law—that of the Income Tax, which was once declared by the Supreme Court to be contrary to the Constitution, and has since been made constitutional by the people, and thereafter declared constitutional by the Supreme Court.

We Americans know all too little of our Constitution; it was the vogue, when I attended school, for the scholars to get some drilling on a knowledge of that pre-eminent work; and it would not be an unbeneficial practice if it were taught equally intensively with the multiplication table and other sound foundations of American learning.

The member of the Exchange must know its Constitution.

Among the questions asked of the intending member of the Exchange is, "Have you read the Consti-

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tution of the Exchange, and do you assent to its provisions?" In the Exchange, at least, there is no laxness as to a knowledge of the instrument which is to guide the actions of the applicant, should he be elected to membership in the Exchange; and an infraction of the Constitution of the Exchange is punishable by the Governing Committee by suspension or expulsion of the offender.

Mutual Protection and Self Interest. Incorporated bodies conduct their business under a Charter and By-Laws; they may or may not have a Constitution. Certain bodies, such as Farmers' Associations, Trades Unions, and the like, not being incorporated, act under a Constitution and By-Laws. Generally speaking, a Constitution sets forth a basis for the organization, an expression of purpose, and a declaration of principles.

The Constitution of Great Britain was founded upon a defensive and offensive basis; defensive of the rights of the barons (and later of the common people), to become offensive if those rights were invaded.

The preamble to the Constitution of the United States declares:

"We, the people of the United States, in order to form a more perfect union, establish justice, insure domestic tranquility, provide for the common defence, promote the general welfare, and secure the blessings of liberty to ourselves and our posterity, do ordain and establish this Constitution for the United States of America."

We note that the States of the Union entered into a compact to "provide for the common defence;" "secure the blessings of liberty;" and thereby "insure tranquility," "establish justice" and "promote the general welfare." To insure the carrying into effect of the agreement, the States surrendered certain rights, and the Nation received certain duties. This was purely a defensive and offensive alliance.

The Constitution of the United States is to a very large extent the reflection of the Declaration of

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Independence, and one of the most significant phrases in that immortal document is that

"all men are endowed with certain inalienable rights, and that among these are Life, Liberty, and the pursuit of Happiness."

To the average mind the terms "independence" and "pursuit of happiness" are inseparable; independence is the power to secure the freedom of one's movements, mental and physical; and without such freedom happiness seems ineffectual.

The Constitutions of Farmer and Labor organizations are purely defensive and offensive.

Through all of these Constitutions, there seems to run a stream of mutual benefit; but, on analysis, the mutual benefit is seen to inure only to those comprised within the organization; the basis of the agreement is that each surrenders some rights in order to secure greatly enlarged benefits to flow from a union for a common cause. In other words, they are based upon mutual protection and self-interest.

It may be a bold utterance, but the speaker feels warranted in saying that the Constitution of the Exchange is not based upon the self-interest or mutual protection of its members. *Nowhere within its confines, and nowhere within its history, is there to be found anything upon which to base the assumption that the Exchange was organized or is conducted upon the idea of mutual protection of its members or in their self-interest, as against the interest of others;* on the contrary, the Constitution is concerned with the idea that the interest of investors and speculators is paramount, and that every conceivable, practical safeguard shall be afforded them; if anything, that the great investing and speculating public is the proper consideration.

The Exchange is composed of 1,100 members; many of these members have associated themselves with non-members into partnerships; and, while the Exchange looks to the individual member as the responsible person, his firm is a recog-

nized entity. These firms conduct business in every legitimate phase of the security business; the Exchange therefore is a combination of individuals pledged to conduct business on a high plane and at a minimum charge for service, and is also a combination of firms engaged in a like business. It therefore partakes somewhat of the nature of a trades-union, with a fixed scale for service, and of the nature of a combination of manufacturers or dealers, engaged in a like business. It, however, differs widely from both the trades-union and the trade organization. At times, it is evident that such associations are interested chiefly in the keeping up of prices, to their own advantage, and without regard to the interest of the public. There is no attempt on the part of the Exchange to force itself as the sole medium for security trading; nothing of a disposition to say: "You deal with us, or you do not deal at all." On the contrary, rather than setting up a standard of prices, the Exchange has been most interested in setting up a standard of morals in business, of service above and beyond that rendered in any business; in a word, its chief object has been, not that its members shall stand together for their own selfish interests, but that those who deal with or through those members shall be assured of 100% service. There is no other organization in the world which gives such care to seeing that the articles dealt in are what they are represented to be, and that a guaranty of title goes with every purchase; nor is there any organization whose scale of prices for the service rendered, considering the values involved and the guaranties given, is so low.

Objects of the Exchange. Article I of the Constitution of the Exchange states as its objects

(1) "to furnish exchange rooms and other facilities for the convenient transaction of their business by its members; (2) to maintain high standards of commercial honor among its members, and (3) to promote and inculcate just and equitable principles of trade and business."

1. The first object has been achieved by the erection of an enlarged Exchange, which was finished in 1903; and by a further enlargement, completed in 1922. What the future of the Exchange may be as to further enlargements is, of course, a matter for decision as the occasion arises; but it may be ventured that, if the Exchange continues its policy of 100 per cent. service to the public, it necessarily must at some future time provide for additional trading rooms. The growth of Listings in the past few years has crowded the available space; the highly enviable position which the Exchange occupies as to the securities permitted to be listed, the quality of service by its members, the protection thrown about the care of customers by the members themselves and by the Committees of the Exchange, all lend color to the feeling that it is as yet in its early growth as to size and importance in the financial world.

Every facility which can be provided is sought to be added to the celerity of filling orders; no expense has been spared in providing pneumatic tube service, there being in use 800 independent tubes connecting every possible part of the trading room, and using 30 miles of such tubes; the ticker machines used are of the most advanced type, and are operated from electrical typewriters installed at convenient locations upon the Floor; there are 567 employees of the Exchange in constant attendance on the Floor; and there are 1100 telephones, connected between the Floor and the offices of members, giving instantaneous provision for the sending of orders and reports of transactions between those points. The Exchange is the only large Exchange in the world which immediately issues news of transactions made thereon; and is insistent upon the instant, and utmost, publicity regarding transactions made within its premises.

2. The second object, while attained in the past, is still the constant object of Committees; high standards of commercial honor are demanded—and are the natural mode of business conducted by the

members. It is rare that a member is recreant to the standards set for him; and when an instance occurs of recreancy, the punishment is swift and severe. There are no indeterminate sentences meted out—no parole boards to mitigate the penalty—no subterfuges of counsel—no appeals to higher courts; the Constitution states

"The findings of the Governing Committee shall be final and conclusive."

3. The third object is, if possible, broader in its scope than the one just referred to; we note that the "high standards of commercial honor" mentioned in the second object are to be maintained "among its members;" but the "promotion and inculcation of "just and equitable principles of trade and business" is not to be confined to members solely—the expression has something of the sweep of the utterance of a well-known Bishop, who, on being reminded that he was not speaking within his own diocese, said "The world is my parish." The influence of the standard set by the Exchange is infectious; it has spread to every properly managed Exchange in America; and it is not too much to say that it has had an effect upon general business practices. It is impossible that an organization, with the standing of the Exchange, should set up such a standard without at the same time becoming the object of emulation by other substantial and far-sighted organizations.

The Public Interest. The Revised Constitution has introduced into its text a phrase which has been for years uppermost in its methods, but has hitherto been unexpressed—"in the public interest."

In the public interest, the Exchange maintains requirements as to securities seeking Listing, which are more thorough than those devised by any Government or other combination; it requires full reports from Listed companies; and it also requires that the certificate sold shall be in all respects exactly what it was represented to be at the time of the sale.

Equally in that interest, the Exchange maintains a high standard for its members and for partners of members. It provides not only that a member may be disciplined for acts committed after becoming a member, but also for fraudulent or dishonest acts committed theretofore; a member is responsible for the acts of his partners, and for those of his employees; the employment of persons considered undesirable must be discontinued.

Members are responsible not only for the conduct of their own business, but also morally for the conduct of non-member brokers for whom the members are doing business; they are forbidden to do business for employees of other brokers, and of certain institutions, except upon the direct consent of the employer. Business connections of members or partnerships which are considered undesirable must be discontinued.

Members are required to make periodical reports of their financial condition, at intervals fixed by a Committee; and this Committee continuously observes the business methods of members, and is empowered to make examinations of their financial condition at will. Reports are required as to securities left in safekeeping with members, with certification thereof by customers. Members are forbidden to misuse the securities of their customers; and securities of customers, even though the customers have assented thereto, must not be pledged, on loans, beyond a reasonable extent.

Committees are empowered to inquire into any practice of members and their firms; no member may assert his legal right, on such inquiries, regarding testimony against himself; he must require his partners and employees to testify, and must produce all books and other records which the Committees require.

Members who participate in market raids may be disciplined; and the Governing Committee may fix a settlement price, where a corner has been adjudged to have been created.

The Constitution of the Exchange and rules adopted pursuant thereto are a part of the terms and conditions of all Exchange contracts. Customers are therefore sure of the conditions which surround contracts for their account made by members; and there can be no equivocation or evasion attempted as to just what terms and conditions obtain on orders executed by members for their customers.

Where non-member brokers receive quotations made on the Exchange, or are correspondents of members, they are required to sign agreements providing that the use of such quotations is open to the inspection of the Exchange; and the exercise of this right has operated to put out of business numbers of brokers who pursued illegal and dishonest brokerage practices.

In November of last year, the Exchange inaugurated a nation-wide campaign against illicit brokerage methods, and the selling of unsafe "securities," which campaign received the unqualified support of President Coolidge; and within the month, President Simmons has issued a further request that members co-operate to the fullest extent with public authorities in disbarring fraudulent brokers and curtailing the sale of fraudulent "securities." The Exchange established its own Securities Frauds Investigating Bureau and, co-operating with the Federal and State authorities and Better Business Bureaus, excellent results have been obtained. As Chambers of Commerce and newspapers throughout the country are also intensely interested in the promotion of ethical business methods and the suppression of fraud, members of the Exchange and their representatives are urged to seek their co-operation in the matter.

It would seem as if no field were left unnoticed by the Exchange in its desire to care for the public interest.

A Great Market. The New York Stock Exchange is one of the great Investment and Specula-

tive markets of the world. The authorities of the Exchange do not deny this fact; but they seek to provide that Investment and Speculation through its channels shall be of a character above reproach. Investment is a term which contemplates little or no risk, a fixed interest return, certainty of return of principal, with little or no thought of profit. Speculation is the risking of money in any legitimate way, in the hope of profit—the regaining of the principal being always in mind. But as we all know, a Speculation may become an Investment, and an intended Investment merely a Speculation, depending on judgment, and conditions. Even ordinary business is but a form of Speculation; as was said by the late Secretary of the Chamber of Commerce:

“The essence of Speculation is risk, and risk is an element in all commercial and credit transactions; if the taking of risks is immoral, then all trade is wicked.”

It is the purpose of the Exchange to minimize, so far as it lies within its powers, the risks attendant upon Investment and Speculation; it seeks to secure the most exact information obtainable regarding securities which it permits to be listed; to compel open and fair dealings in those securities; to have a high standard of membership; to see that that membership is above financial reproach or suspicion; to reduce to the minimum the possibility of failure among its membership; and to see that such non-member brokers as receive quotations or are permitted to be correspondents of members give honest service and complete information regarding transactions done by them. The United States is probably the richest country in the world, and the American people probably of all peoples the greatest speculators; this may be attributed to the enormous gains arising within recent years from modern inventions, the growth of the country, and the desire for independence already alluded to.

Purposes of the Revision. The Special Committee on Revision of the Constitution was appointed

on January 6, 1922; and it completed its labors on April 22, 1925; during that period, it had compiled the decisions of the various Committees of the Exchange, since the Revision made in 1902, a work which occupied every phase of Stock Exchange procedure during that lengthy and constructive period. It will be remembered that the business of the country took enormous strides within the two and a half decades comprised in those years; that the wealth of the United States had increased from about 100,000,000,000 of dollars in 1900 to about 300,000,000,000 of dollars in 1925; that the number of incorporations had grown in like if not greater proportion; that the number of holders of stocks in corporations had multiplied manifold; and that the Exchange had become the standard for dealings in securities.

During the twenty-three years since the last previous Revision, numerous changes had been made in laws relating to securities; there was a constantly increasing feeling that the well-being of the public should be conserved through its protection from various fraudulent issues, and by honestly administered brokerage practices. While the Exchange itself has always insisted upon the strictest accountability of its members for proper business dealings, its influence in the security market was not sufficient at the outset of the twentieth century to have the weight with respect to outside practices which it has now attained. For twenty years prior to that time, the Exchange had carried on its warfare against crooked brokers; however, its efforts were soon to receive recognition in the passage of anti-bucketshop laws and other statutes against wrongful issues of stocks and equally wrongful practices in security selling.

During the twenty-three years in question, the Exchange had adopted numerous resolutions, which strengthened its attitude against illicit brokerage methods; other resolutions, requiring greater publicity with respect to security issues; and still others

as to the methods of its members in the handling of accounts and calling for greater circumspection with respect to those for whom such members might do business. Provision was made for the greater volume of business, which both the growth of the country and the driving out of crooked brokers, would bring to legitimate markets. All of these matters were necessarily considered as a part of the Revision.

There is today a plethora of laws, a multiplication of statutes, and a tendency in many quarters to meet some new phase of an old situation by the passage of further laws; and a general codification of law would not be an easy matter, although of undoubted value. The Exchange, happily, has been faced with no such arduous task; its rules and dictums have been few, and comprehensive; there is a rule that *any act* which the Governing Committee may consider as detrimental to the interest and welfare of the Exchange shall be punishable as that Committee may determine; there is another rule that *any conduct* or proceeding considered to be contrary to just and equitable principles of trade or business is also punishable; and there is a rule that *any act* adjudged to be fraudulent is punishable. These have been the foundation rules of the Exchange for many years, and it will be seen that they have in view the widest possible scope and latitude toward the prevention of acts which all right-minded men should condemn.

Of course, with the changes in markets, the broadening scope of the Exchange, the growth of the business upon its Floor, the increased number of Listings, the enlarged space recently added to the Exchange building, the adding of pneumatic tube service, the installation of quicker and more modern tickers, some changes necessarily have had to be made in trading regulations; there was also the justifiable feeling that in a broad, general sense, the public has been looking and is still looking to the Exchange for the setting-up of a standard of

security dealings which shall afford the best possible service and be so high as to be above reproach.

Changes Made by the Revision. The first great change noted in the Revision is the separation of the former Constitution and resolutions, into a comparatively compact Constitution, and Rules. The Constitution, itself, has to do with certain matters, which may be summarized as follows:

The objects of the Exchange:

The Government of the Exchange, including the powers of the Governing Committee; the powers and duties of other Committees; and the duties of officers of the Exchange;

Admission to, and retirement from Membership;

Definitions of Members' Contracts and Exchange Contracts;

Measures for securing the moral purposes of the Exchange;

The Commission law of the Exchange;

Partnerships, and Associations of Members;

The Death benefit;

The Stock Clearing Corporation.

The Rules have mainly to do with methods of doing business, both upon the Floor of the Exchange, and in offices of members; they are subdivided into chapters, bearing upon

Dealings upon the Exchange;

Exchange of Tickets and Comparisons;

Payment and Delivery, and Settlement of Contracts;

Closing of Contracts;

Marking to the Market, and Mutual Deposits;

Closing of Books and Interest on Bonds;

Commission rates, under certain circumstances;

Advertising;

Visitors to the Exchange, and Communications;

Arbitrage, and Continuous Quotations;

Members Dealing for their own Account;

Conducting of Accounts;

Wire and other Connections;

Miscellaneous Prohibitions;

Semi-annual Financial Statements;

Offices, and Employees thereat.

These Rules cover every form of operation connected with the business of members; the greatest care has been exercised to make the language of the Rules simple and direct. As the Rules are to form part of every Exchange Contract, it is highly desir-

able that they shall be understandable, and unequivocal; and running through them is seen the intention that the customer shall know his rights, and that those rights are protected. As has been said hereinbefore, the *rights of brokers* are not the matter of interest in the Constitution and Rules; their duties and obligations are carefully set forth—their rights are subordinated to those for whom they act.

If anything, the Revision places upon members greater obligations and larger duties than ever heretofore; indeed, it would be hard to conceive of a code which requires more than is now required; and judging from the past, should there arise a situation necessitating further obligations and duties upon the members of the Exchange, there can be no question but that they would be imposed by the Governing Committee.

In addition to the previous extensive powers of the Governing Committee, there has been added a sentence of but three lines and of but twenty-five words, as follows:

“In the exercise of its powers, it may adopt such rules, issue such orders and directions, and make such decisions as it may deem appropriate.”

Can more far-reaching language be devised? Those who are interested in the Exchange, as members, as employees of members, as employees of the Exchange, as investors or speculators, or in any other capacity, should give careful study to the Constitution of the Exchange; it is a document of high purpose; it has been carefully revised to meet present needs, yet with a view to the future; and is worthy of consideration as a system of rules, a code of business ethics, and a standard of dealings.

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