MEMORANDUM OF LAW

Re: Multiple Trading Rule

This memorandum is concerned with the Commission's authority to direct the New York Stock Exchange to alter or amend a ruling recently published by its Committee on Member Firms, commonly referred to as the "Multiple Trading Rule". The effect of this ruling is to subject to discipline any members of the Exchange who act as odd-lot dealers or specialists or otherwise publicly deal for their own account on other exchanges in securities listed on the New York Stock Exchange, notwithstanding that such members are also members of such other exchanges and that these securities are lawfully registered under the Securities Exchange Act of 1934 or are admitted to trading privileges on those other exchanges.[1]

[1] The text of the ruling is: "…any member, allied member or member firm acting as an odd-lot dealer or specialist or otherwise publicly dealing for his or its own account (directly or indirectly through a joint account or other arrangement) on another exchange in securities listed on the New York Stock Exchange, shall be subject to proceedings under Section 8 of Article XVI."

I.

THE SCOPE OF THE COMMISSION'S POWERS UNDER SECTION 19(b) OF THE ACT

A. A Determination of the Scope of the Commission's Powers to Order the "Multiple Trading Rule" to be Altered or Supplemented should be Delayed until the Close of the Hearing.

For the reasons set forth below we consider the Commission's power to order the "Multiple Trading Rule" to be altered or supplemented to the extent necessary or appropriate for the protection of investors or to insure fair dealing in securities traded in upon the exchange or to insure fair administration of such exchange, to be demonstrably clear. Nevertheless, it is our considered judgment that this determination, involving as it does the exercise of a judicial function -- the interpretation of a statute, must be delayed until the facts of the case in which the interpretation is to be applied is before the Commission.[2]

A determination of the Commission's authority should not be made in abstracto. The "Multiple Trading Rule" is concerned with intricate and subtle problems of modern finance. The interplay of important economic factors with which it is concerned are empiric matters; they should not be judged in an unreal atmosphere. Responsibility is not an inexorable quality; in crucial cases it resolves itself into a judgment upon facts. To determine the scope of the Commission's obligation here in the absence of a record of facts might well lead to dialectics unrelated to actualities. It is submitted that no premature determination of the Commission's

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[2] While the Commission has before it the facts as set forth in the staff report, we think that these facts should be tested in a public proceeding in which interested persons can question the accuracy of the facts therein set forth before they are accepted by the Commission for the purposes of this case.

obligation should be made; the determination should be made only after a record of facts is before the Commission and after the impact of these facts upon the statutory standards can be evalued.

Happily, the Commission to our knowledge has never consented to determine its statutory authority in a particular matter until a record of facts has been made. We find in this proceeding no reason justifying the Commission in departing from its settled practice. Indeed, we submit that this question cannot be finally disposed of by the Commission in advance of hearing the facts since, in any event, the Commission's authority to require the change in the New York Stock Exchange's rule is conditioned upon the Commission's determining that the change is "necessary or appropriate for the protection of investors or to insure fair dealing in securities traded in upon such exchange or to insure fair administration of such exchange." Until such a factual showing is made it would be an empty gesture to make a determination of the extent of the Commission's powers under Section 19(b).

B. The Statutory Provisions

The instant proceeding is one brought pursuant to Section 19(b) of the Act. The provisions of that Section are:

> "The Commission is further authorized, if after making appropriate request in writing to a national securities exchange that such exchange effect on its own behalf specified changes in its rules and practices, and after appropriate notice and opportunity for hearing, the Commission determines that such exchange has not made the changes so requested, and that such changes are necessary or appropriate for the protection of investors or to insure fair dealing in securities traded in upon such exchange or to insure fair administration of such exchange, by rules or regulations or by order to alter or to supplement the rules of such exchange (insofar as necessary or appropriate to effect such changes) in respect of such matters as . . . ." (Underscoring ours)

And then follow thirteen items dealing with various aspects of security transactions, including such matters as safeguarding financial responsibility of members; restrictions on trading within a period after primary distribution; listing or striking from listing, hours of trading; "manner, method and place of soliciting business"; commissions, listing charges; "odd-lot purchases and sales"; and several others which we will omit; finally concluding with an item (13) reading "similar matters".

It is significant that this section gives the Commission authority not alone over rules affecting the twelve items specifically enumerated (which themselves are introduced by a "such matters as" phrase), but extends its authority over "similar matters" as well. Thus it is apparent from the section that the Commission's power extends not only to the enumerated items but also to matters that are like or similar to the enumerated matters even though they are not identical with them.[3]

In interpreting the power vested in the Commission by Section 19(b) consideration must be given not alone to its provisions, but the policy of the Act, relevant legislative history,[4] and controlling principles of statutory construction as well. The policy of the Act is expressed in Section 2 which recites that for reasons thereafter enumerated transactions in securities upon securities exchanges and in the over-the-counter markets are affected with a public interest, which makes it necessary to provide for regulation and control of such exchanges and "of practices and matters related thereto", and "to impose requirements necessary to make

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[3] This construction is amply supported by precedents. See Traders' Insurance Co. v. Dobbins & Ewing, 114 Tenn. 227, 86 S. W. 383, 385; Charles Behlen Sons' Co. v. Ricketts, 30 Ohio App. 167, 164 N.E. 436; Ventura County v. Clay, 112 Cal. 65, 44 Pac. 488, 491; In re Hull, 18 Idaho 475, 110 Pac. 256, 257; Ex parte Haney, 51 Tex. C. R. 634, 103 S. W. 1155.

[4] Cf. United States v. Dickerson, 310 U.S. 554; United States v. American Trucking Associations, 310 U.S. 534.

such regulation and control reasonably complete and effective, in order to protect interstate commerce . . . to insure the maintenance of fair and honest markets in such transactions."

Turning to the legislative history we find that the Securities Exchange Act represents an endeavor by Congress "to create a fair field of competition among exchanges and between exchanges as a group and the over-the-counter markets, and to allow each type of market to develop in accordance with its natural genius and consistently with the public interest."[5]

In approaching the precise scope of the Commission's authority under Section 19(b) a cardinal rule of statutory construction must be recalled, viz., that remedial statutes are to be liberally construed in order to effectuate their remedial purpose. See Securities and Exchange Commission v. Crude Oil Corporation, 93 F. (2d) 844 (1937); Securities and Exchange Commission v. Universal Service Association, 106 F. (2d) 232 (C.C.A. 7, 1939); Securities and Exchange Commission v. Associated Gas and Electric Company, 99 F. (2d) 795 (C.C.A.2, 1938); Securities and Exchange Commission v. Payne, decided November 15, 1940, (S.D.N.Y.).

C. The Subject Matter Involved Falls within the Statutory Provisions.

Among the specific items enumerated in the Section we find included the "manner, method, and place of soliciting business". The Multiple Trading Rule by prohibiting its members from acting as odd-lot dealers or specialists on the regional exchanges operates to curb their rights to solicit business. In the first instance the Rule prevents them from soliciting on a regional exchange any business in dually traded securities for execution on such regional

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[5] S. Rep. No. 1739, 74th Cong. 2d Sess., p. 3.

exchange. Moreover, whenever a broker-dealer advertises himself to be a member of several exchanges he is, in effect, soliciting business for execution on those exchanges.[6] It, therefore, follows that the new Multiple Trading Rule deals to a large extent with the same subject matter as at least one of the matters enumerated in the Section.

Item 11 refers to "odd-lot purchases and sales". As will be seen, the new Multiple Trading Rule deals to a very great extent with a problem related directly to "odd-lot purchases and sales". Under the Rule, members of the New York Stock Exchange are forbidden to buy and sell odd-lots in dually traded securities on the regional exchanges. Here too, the Rule deals with the same subject matter as is contained in one of the enumerated matters in Section 19(b).

Even if it is felt that the ruling does not deal with the same matters as those specifically enumerated in Section 19(b), it is undeniable that it deals with manner similar thereto.

Another consideration is that the Multiple Trading Rule represents an attempt on the part of the largest and most powerful exchange to deal harshly with other exchanges and to make oppressive use of its powers to the detriment of smaller exchanges in other states and of the public they serve.[7] This consequence thwarts the expressed endeavor of Congress "to create

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[6] Query: If this ruling remains should members of the New York Stock Exchange go on advertising themselves as members of other exchanges unless they disclose the New York Stock Exchange's restrictions upon those other memberships? This query suggests that the New York Stock Exchange is really seeking to condition and restrict the privileges of its members as members of other exchanges in respect of securities which are as validly admitted to those exchanges as to the New York Stock Exchange.

[7] Query: Is this ruling princiapply to the advantage of the three or four New York Stock Exchange odd-lot dealers and to the disadvantage of all the other New York Stock Exchange members who might wish to deal in odd-lots on regional exchanges and therefore is it fair administration within the New York Stock Exchange itself?

a fair field of competition among exchanges and between exchanges as a group and the over-the-counter market, and to allow each type of market to develop in accordance with its natural genius and consistently with the public interest".[8] It is significant that (1) the securities in which trading is restricted by this ruling are securities lawfully admitted to trading on the regional exchanges as well as on the New York Stock Exchange, and (2) the persons against whom this ruling is directed are members of both exchanges. The inevitable tendency of this ruling will be to establish a virtual monopoly of trading on the New York Stock Exchange in securities listed on several exchanges.

As we stated above the recitation of policy in Section 2 of the Act is a guide in interpretating Section 19(b). Several of these matters referred to therein are involved in the instant problem. Regulation lacking power to deal with the practice of multiple trading would not be "reasonably complete" and it could not "protect interstate commerce", which is obstructed by this rule. As a consequence of the ruling, the choice of the public as to where to trade is restricted, costs to the public are increased, and its convenience impeded. The claim that regulation which cannot deal with such a situation is "reasonably complete", is unconvincing.

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[8] S. Rep. No. 1739, 74th Cong. 2d Sess., p. 3.

II.

CONCLUSION

It is concluded that the Multiple Trading Rule is concerned with a subject matter falling within the gamut of the Commission's powers under Section 19(b) of the Act and that the Commission in the fulfillment of its obligation to the public and the regional exchanges must order the Multiple Trading Rule to be altered or supplemented to the extent found necessary to effectuate the purposes of Section 19(b) of the Act.